TWENTIETH CENTURY COMMON SENSE AND THE AMERICAN CRISIS OF THE 1960's

BY THE EDITORIAL STAFF OF
AMERICAN INSTITUTE FOR ECONOMIC RESEARCH
UNDER THE DIRECTION OF E. C. HARWOOD

Published by

AMERICAN INSTITUTE FOR ECONOMIC RESEARCH
A Scientific and Educational Organization
Great Barrington, Massachusetts

Price: One Dollar
Three Copies for Two Dollars, Ten Copies for Five Dollars

330.973
A5125tw
c.3

UNIVERSITY
OF FLORIDA
LIBRARIES

AMERI **SEARCH**

Ame ndent scien-
tific and oncentration
of wealt pted in its
publicati d primarily
by the sn ng members
and by r

Sinc te has been
to provic dable infor-
mation ggests that
informati seful when
they com rests, either
commerc

Stri neither the
Institute m organiza-
tions or of Institute
research. Institute accounts are open to the public, and a report of Institute activities, published periodically, is available without charge.

The Institute administers an undergraduate scholarship program in order to encourage exceptionally talented young people to seek a career in the social sciences. About 200 scholars in colleges and universities throughout the country are participating in this program. The most successful of them, and other qualified candidates, become eligible for the Institute's graduate fellowship program, which provides graduate training in modern scientific research at the Institute and leads to the Ph.D. in economics at any participating college.

The Institute's research is planned to help individuals protect their personal interests as well as those of the Nation. The industrious and thrifty, those who pay most of the Nation's taxes, must be the principal guardians of American civilization. By publishing the results of scientific inquiry, carried on with diligence, independence, and integrity, American Institute for Economic Research hopes to help those citizens preserve the best of the Nation's heritage and choose wisely the policies that will determine the Nation's future.

Institute publications are listed on the inside of the back cover.

Digitized from UF. Surveyed to Internet Archive

TWENTIETH CENTURY COMMON SENSE AND THE AMERICAN CRISIS OF THE 1960's

BY THE EDITORIAL STAFF OF
AMERICAN INSTITUTE FOR ECONOMIC RESEARCH
UNDER THE DIRECTION OF E. C. HARWOOD

AMERICAN INSTITUTE FOR ECONOMIC RESEARCH
GREAT BARRINGTON, MASSACHUSETTS

330.973
A5125tw
c.3

NOTE

Some of the material in *Twentieth Century Common Sense and the American Crisis of the 1960's* has been collected and revised from earlier publications of the Institute. The content of Chapters I and II was published in a Special Bulletin in March 1958. The substance of Chapter III comes from a Special Bulletin published in August 1950. It subsequently was incorporated in a book called *The Counterrevolution, American Foreign and Domestic Policy and Economic Aspects of National Defense* (by the Editorial Staff of the Institute). Chapters IV through X, the "American Crisis" series of articles, first appeared in *Economic News,* Volume III (1960).

Copyright 1960

(Reprinted in 1961)

by

AMERICAN INSTITUTE FOR ECONOMIC RESEARCH

Printed in the United States of America
THE BEN FRANKLIN PRESS, Inc.
Pittsfield, Massachusetts

CONTENTS

		Page
PREFACE		4
Chapter I.	What Must We Do To Survive?	5
Chapter II.	Learning From Experience	20
Chapter III.	The Counterrevolution	33
Chapter IV.	First Steps Toward a Solution	43
Chapter V.	Stand Still, Little Lamb, To Be Shorn	49
Chapter VI.	Can Farmers Be Saved From Their Politician Friends?	56
Chapter VII.	Putting Friends in Socialist Straitjackets	63
Chapter VIII.	Can Our Republic Survive?	71
Chapter IX.	Economic Aspects of a Survival Program	79
Chapter X.	Coping With the American Crisis of the 1960's	87

Charts:

U. S. Gold Reserve vs. Net Foreign Short-Term Claims	44
Required Gold Reserve for U. S. Money-Credit System vs. Actual Gold Reserve After Foreign Claims	44
Sources of Purchasing Media	90-91

Tables:

How America's "Forgotten Men" Have Contributed to the "Success" of Inflation	51
Family Incomes After Federal Income Taxes	81

-22-64 Anonymous Gift

PREFACE

In the months and years of prolonged crisis that preceded the birth of our Nation, Thomas Paine's series of essays called "The American Crisis" was published. Many Americans, and probably citizens of other nations as well, from that time to the present, have found inspiration in its opening words, "These are the times that try men's souls." Many who observed the influence of those essays, including Washington, Franklin, and Jefferson, credited the author with a major share in the success of the War of Independence.

Earlier the same author's remarkable pamphlet *Common Sense* (published in January 1776) had pointed the way toward independence and, perhaps to a greater extent than the writings of any other man, convinced Americans that they should initiate a great revolution in the affairs of mankind, a revolution later given more definite form and direction by the Constitution of the United States.

Once again the Nation is passing through years of crisis, years that will decide whether we shall continue toward the goals of the great revolution or turn back from pursuit of those goals. In the past, when the Nation has been endangered, its youth have responded with vigor to the call to arms. But today the principal danger to the Nation cannot be combated by a call to arms. Now our great need is effective economic and other social research, a field in which older and inadequate methods of inquiry must be replaced by modern scientific methods. Man seems to have reached a point in his evolution beyond which the requisite for progress is more effective use of his brain.

Our title has been borrowed from Thomas Paine but is not, like the *Common Sense* of 1776, a call to arms; rather, it is an invitation to think. Perhaps the common sense of the future, developed by scientific research on the problems of men, will appeal only to an independent and thoughtful minority at first. But we remind the reader that minority opinion does count and that some of the Nation's most critical problems exist because small minority groups have been all too effective in getting their way. The independent voter (whether registered under a party label or not) holds the balance of power nearly everywhere in the United States. Perhaps a republic can be saved by the voting influence of a well-informed, public-spirited minority as readily as it can be destroyed by the self-seeking of smaller minorities who are not effectively opposed.

THE EDITORIAL STAFF

I.

WHAT MUST WE DO TO SURVIVE?

What must we do to survive? For Western civilization and especially for that portion of it within the United States, this is the crucial question of our times. In attempting to answer this question we propose to review pertinent economic facts of the past and present, to summarize the Nation's long-term objectives, and to point out the route towards those objectives.

Pertinent Facts

For many decades the economic growth of the United States so far surpassed that of other countries that our Nation became the industrial colossus of the world. The great European industrial empires, England, Germany, and France, far in the lead as industrial nations only a century ago, also have grown, but so slowly in relation to the expansion of industry in the United States that they are not even close seconds in the race today. Measured by the production of steel, a basic commodity in a modern industrial society, the United States in recent years has produced nearly 5 times that of the leader among the three others mentioned and about double their combined total.

From its earliest days our Nation has repeatedly suffered from the adverse effects of an unsound money-credit system. The days of "wildcat" banking in the first few decades of the 1800's were notorious; and, even after the national banks were well established in the decades following the Civil War, the elementary lessons of sound commercial banking had not been learned. In the 1870's and 1890's great depressions with many hundreds of bank failures were the aftermaths of unsound credit expansion, of the inflationary creation of excess purchasing media by the Nation's banks. Again in the first decade of the present century a financial panic and depression followed serious abuse of the banking system with the resulting failure of hundreds of banks.

These harsh lessons were not ignored, however. At long last, advantage was taken of the example provided by nearly a century of relatively sound commercial banking in England. After prolonged study by a National Monetary Commission and equally prolonged consideration by Congress, the Federal Reserve System of regional central banks and member banks was begun in 1914. For the first time in its history, the Nation had a banking system based on recognition and application of the basic principles of sound commercial banking.

Whether or not the new banking system might have functioned well, limiting overexpansion during prosperity booms and as a consequence lessening the severity of subsequent recessions, we do not know. Before the new system was well established, the United States had entered World War I. Once again the politically expedient course, inflation, was chosen; and into the discard went the principles of sound commercial banking on which the new system had been based.

The wartime inflation was continued into the early postwar years until drastic deflation seemingly became the only alternative to a further skyrocketing of prices generally. The deflationary collapse of 1920-21, again with hundreds of bank failures of course, testified to the preceding inflationary misuse of the banking system.

So extensive was the collapse in prices that the political pressure for supporting commodity prices became great. The managers of the Federal Reserve System, including especially the then influential Governor of the New York Federal Reserve Bank, determined to try an easy-money policy in order to support prices at higher-than-prewar levels. Other factors, such as an attempt to aid England in restoring the gold standard, also were involved. The net effect of the prolonged easy-money policy through most years of the 1920's was another great inflation with its inevitable aftermath, the great "boom and bust" at the end of the decade. Nearly one-third of the Nation's banks failed in the next 3 years, thereby confirming once again that the basic principles of sound commercial banking had been generally ignored.

In order to understand what followed we must turn our attention to another aspect of economic developments. During most of the Nation's prior history vast areas of free land available for the taking had provided a safety-valve in times of depression. Many of the unemployed could follow the advice to "go west, young man, go west," and many others could rely on "the folks back home" on nearby farms. Most of the population still had roots in the land, parents, brothers, uncles, or cousins on whose farms food, at least, was available in the worst of depression periods. During the most extensive depression in the Nation's history, that of 1873-1879, few people lacked the necessities of life. Even during the severe depression in the 1890's, only a small portion of the unemployed became desperate for food.

But by the 1930's the situation had altered greatly. The absence of free land accentuated the privileged position of those who enjoyed the natural resource monopoly privilege, and the city proletariat, one or two generations removed from the Nation's farms, had nowhere to turn. A situation long prevalent in Europe finally had become commonplace in the United States.

Under such circumstances the pressure for desperate measures be-

came overwhelming, or at least so the politicians of the times concluded. Instead of probing once again for underlying causes of the difficulties, as was patiently done after the depression at the turn of the century, the politicians hastily treated symptoms with one obvious result, prolonged depression.[1]

So unsuccessful were the efforts to cope with the Great Depression of the 1930's that during the whole decade the smallest number of unemployed was 7,700,000 in 1937. From this amount the total increased to 9,500,000 in 1939. Throughout the 1930's approximately one-fifth of the labor force was unemployed despite the notion, widely prevalent today, that the New Deal somehow remedied the Great Depression.

Then in the 1940's another great war ended the problems of depression and substituted others equally familiar. Once again, monetization of public debt was adopted as the expedient means of financing the war effort. By 1946, nearly $70,000,000,000 of Government debt had been monetized by stuffing Government bonds into the commercial banks, which created new Treasury accounts in payment for the bonds.

As the Treasury wrote checks to pay for munitions, etc., this huge amount of inflationary purchasing media was transferred to businesses and individuals. Fortunately, much of the total purchasing media, about half, was held unused either as hoarded currency or as idle checking accounts, apparently because new automobiles and many other consumer goods were not available and because new equipment and materials for new plants were not available for purchase by businesses. Consequently, the effects of the great inflation were largely postponed until after World War II.

If the huge total of inflationary purchasing media hoarded (or held inactive in checking accounts) during World War II had been spent almost immediately after the war, the resulting rise in prices generally would have been far more rapid than the rise that did occur. (As usual when resort is had to price controls, many of the price rises prior to the abandonment of futile price controls were concealed from the statisticians by quality deterioration, etc.) At least two factors were responsible for the relatively slow use of the hoarded purchasing media.

First, countless individuals including many managers of corporate businesses expected a postwar depression within a few years. In fact so widespread were the fears of a depression in 1946 that the Federal Government was urged to adopt strong measures in order to cope with anticipated mass unemployment. For several years thereafter, many who

[1]Lest the reader assume that the facts cited are the products of selectively imaginative hindsight, it seems desirable to add at this point that the authors are prepared to offer proof of all such statements. Readers who desire such references in detail may have them on request. They will include many economic analyses that correctly *predicted* the outcome of measures adopted by Congress.

remembered the 1920-21 experience held funds idle in the expectation that a depression would provide better opportunities for those who wanted to buy.

The second factor responsible for the slow rate of dishoarding was the time required for factories to convert to peacetime output and to produce enough for the postwar demand. For a few years demand for such items as automobiles, housing, some types of machinery, etc. was greater than the existing productive capacity could satisfy. Moreover, the Korean war, although relatively minor in its economic effects, again restricted to some extent the availability of numerous items desired for civilian consumption and for business.

As the hoarded or idle inflationary purchasing media were gradually used in the postwar years, the amount available was supplemented by the monetization of increasing private debt (largely real-estate loans and installment loans) by the commercial banks. Thus the amount of inflationary purchasing media in circulation was almost continually increased, except for minor interruptions in 1948-49, 1953-54, and 1957-58.[2]

The great inflationary development, begun during World War II and continued through subsequent years, had the usual chain of effects. Although on a larger scale in several respects, these effects duplicated those experienced several times during the Nation's history. They may be summarized as follows:

1. Effective demand (that is, desire implemented by purchasing media) during most of the period and for most types of products exceeded the supply of processed things at prevailing prices.

2. Therefore, prices generally rose with a resulting succession of "windfall" profits to most businesses. (In some instances, certain prices that otherwise would have fallen were supported at relatively high levels by the great inflation.)

3. With the encouragement of increasing demand and partly by using the funds that "windfall" profits provided, productive capacity was greatly expanded, so much so in the later years of the period that, as in the 1920's, the expansion of plant and equipment itself became a major factor in the growing intensity of the business "boom."

4. Organized labor, stronger than ever before, demanded a share of the "windfall" profits. Business management acquiesced, in some instances perforce, in others believing or hoping that the conditions

[2]Some of the increasing real-estate and consumer loans were *not* inflationary; that is, part of the loans did *not* result in the creation of new and inflationary purchasing media, because the funds loaned were derived from current savings rather than from new credits to demand deposits or checking accounts. For a more detailed discussion, see E. C. Harwood, *Useful Economics,* American Institute for Economic Research, fifth edition, 1960, Chapters VII and VIII.

creating ever-increasing profits would continue indefinitely. Thus, for example, assembly-line workers in Detroit (as well as workers in the basic steel and construction industries) saw their prewar wages more than quadrupled (including fringe benefits) while teachers in the public schools fought a losing battle to have salaries increased as rapidly as the cost of living rose. In fact, so great have been the wage increases in *some* industries profiting most from inflation that the armed services have been unable to retain vitally needed technicians who leave after one or two enlistments for the far better pay available elsewhere.

5. Of course, most owners of common stocks and real estate profited from the prolonged inflation. The great increase in the value of such holdings and in the incomes from them reflected in substantial part the shift of real wealth from retired individuals dependent on pensions, from holders of life insurance, savings bonds, and savings deposits, and from that large portion of the population whose incomes were relatively fixed or who could not obtain sufficient increases to offset the continuing depreciation of the dollar (rise in prices).[8]

6. The easily-won profits for businesses of many types and for many individuals encouraged speculative expansion in various segments of the economy. For example, new office buildings in New York and other cities were constructed in the later years of the recent boom period on a scale rivaling that of the ill-fated 1920's; otherwise competent business executives with their eyes on "pie in the sky" in the 1960's embarked on over-ambitious expansion programs.

7. Perhaps most unfortunately situated are the millions of wage earners enabled by the subtle robbery of their own and others' pension funds, life insurance, etc. to claim a higher standard of living in the form of the new cars, new homes, etc., thus made available to them on the installment plan. Encouraged to incur debt beyond their ability to pay under less favorable circumstances, many such individuals are finding that the growing population supposed to perpetuate increasing prosperity includes their own children (more numerous because of prosperity's optimism) whose needs only make more burdensome the debt so hopefully assumed.

8. By no means the least of inflation's effects has been the subsidizing of that proficient spendthrift, the Federal Government, with increasing taxes seemingly almost painlessly extracted from continually increasing personal incomes and business profits. The huge sums so easily obtained have fostered national delusions of economic grandeur. Grandiose plans for aiding other nations and silly schemes for remedying

---

[8]Government-sponsored "theft" via inflation has taken nearly $200,000,000,000 worth of real wealth (goods and services) from holders of life insurance and savings bonds, savings depositors, etc., since 1940 (see table on page 51).

our own internal problems such as those of agriculture have been fostered by politicians seeking votes and by exuberantly confident bureaucrats who have, it must be conceded, at least the ability to spend money rapidly if not wisely. In fact, so lavish was the giving and "lending" to other nations that, *in addition* to providing Cadillacs for oil princes in Saudi Arabia and an infinite variety of other goods from armament to zippers, we managed in a single decade to give foreigners demand claims on nearly all of the Nation's basic gold reserves.

We know that the inflation (creation of excess purchasing media) in recent years has been the greatest in the Nation's history. Fortunately, speculation on margin, in the stock market at least, has been much less than that of 1928-29 although the expansion of inflationary private debt in recent years has exceeded that of any earlier period. That there are many serious distortions within the economy seems obvious; such always has been the situation after prolonged inflation.

Much of the recent inflation was attributable to the monetization of Government debt. Such inflation is not subject to the automatic deflation that results from widespread bankruptcies and the collapse of innumerable private debts. Consequently, only part of the present inflation is as vulnerable as that of 1929, and precisely how vulnerable that part is cannot be ascertained until the recession testing process has carried further than it has in recent years.[4]

In any event, questions about this aspect of the problem will be answered in the years ahead. If the deflation of private debt becomes extensive, a depression as severe as that of 1937-38 is well within the range of possibilities, but we do not expect a depression such as that of 1929-32, primarily because the inflation reflecting monetization of Government debt is not vulnerable to forced deflation via private bankruptcies.

The Nation's Long-Term Objectives

We now turn to consideration of the Nation's long-term objectives. Unless our objectives are clearly stated and kept constantly in mind, we cannot reasonably hope to make wise day-to-day decisions regarding the route to be followed. The four principal pertinent objectives stated and implied in the Nation's basic plan, the Constitution of the United States, may be summarized as follows:

1. A society so organized by Constitution, statute, and custom that each adult member will be continually influenced to cooperate

[4]We believe that the huge total of private debt incurred in recent years ($400,000,000,000 since 1945) includes a small percentage of vulnerable loans reflecting unwise borrowing. Only 3 percent of it would equal the loans for stock speculation on margin in 1929, and we suspect that even more may have been unwisely incurred.

with others by serving their needs as they in turn are under a like compulsion to serve his, thus indirectly serving their own. The end desired is perfect cooperation, and the means clearly implied in the Constitution is free competition.[5] "Free" implies not the chaos of anarchy but operations under "rules of the game" intended to preserve the maximum freedom for all, large and small, among the providers of economic goods and services.

2. Within the society, freedom for individuals to plan and choose their occupations, other activities, and goals.

3. For all men, equality of opportunity to find their places in the economy and seek their goals.

4. To each individual, the fruits of his own labors not only as an incentive and reward but also, *and even more important for the Nation as a whole,* so that the individual (or business) who demonstrates capacity to serve his fellow citizens most effectively will have increased means at his disposal, enabling him to become more and more effective on a larger and larger scale.

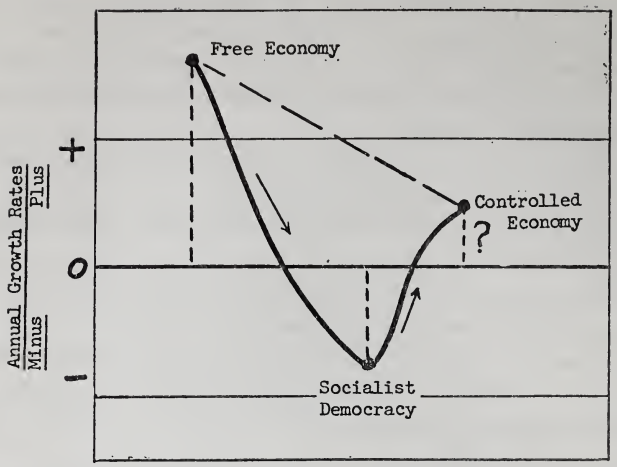
The pursuit of these four objectives will foster the achievement of a fifth, which is of vital importance today, namely, a rate of economic growth that will ensure a widening of the present gap between the industrial power of the United States and that of Russia.

This last objective warrants more detailed discussion in order that it may be fully understood. For this purpose the diagram on page 12 illustrates the discussion that follows. It seems desirable to emphasize that the diagram does not attempt to represent accurately in detail the relative differences in growth rates between free, socialistic, and communistic economies. However, the historical record clearly establishes that a free economy grows more rapidly than a controlled economy and that a socialistic economy (without strong-man controls) has a negative rate of growth, in fact cannot even survive in the long run (for example, the fate of the early Plymouth Colony and more recently the effects of even partial socialism on Great Britain, France, and other nations).

Referring now to the diagram, the annual growth rate of a free economy is indicated as a plus value signifying a compound rate of growth year after year such as that experienced by the United States for much of nearly two centuries. The only prolonged departures in the United States from well-sustained economic growth have occurred following major interferences with its relatively free competitive economic system. For the latter part of the 19th century in particular, the record

[5]For a detailed discussion pointing out that "free competition" is simply a different name for voluntary cooperation and that such free competition is essentially different from war, see Appendix C "Free Competition is Voluntary Cooperation" of the book, *Useful Economics,* by E. C. Harwood, American Institute for Economic Research, fifth edition, 1960.

COMPARATIVE ANNUAL GROWTH RATES,
FREE VS. CONTROLLED AND
SOCIALISTIC ECONOMIES



of industrial production is sufficiently accurate and the conditions of relative freedom were adequate to establish clearly that such an economy enjoys a high rate of growth.

Some readers may wonder whether the lessons of the American historical experiment are applicable elsewhere, for example in Europe. The experience of Western Germany since World War II provides a convincing demonstration that a relatively free economy assures rapid growth even when hampered by the prior existence of extensive controls and by the wartime destruction of its means of production.

The annual growth rate of an economy operating under a socialistic dictatorship such as Communist Russia, i.e. of a ruthlessly controlled economy, is shown as a smaller plus value. Whether or not its annual rate of growth will be a plus value in the long run is indicated by a question mark. Evidently a positive rate of growth is possible for a prolonged period, but there is as yet no proof that it will last for centuries and will pervade the entire economy. That the annual growth rate of such an economy, *in its entirety,* is less than that of a relatively free economy is well established.[6]

Below the zero rate of growth and indicating negative growth or economic decay and retardation, we show Socialist democracy. This is the situation where the state seizes all factories and other wealth and distributes the goods currently produced according to some plan specified from time to time by the legislative branch of government. No economy

[6]See, for example, G. Warren Nutter, *Some Observations on Soviet Industrial Growth,* Occasional Paper 55, National Bureau of Economic Research, New York, 1957.

operated in this manner *without* dictatorship and ruthless controls thus far has been able to survive. Numerous economies have experimented with varying degrees of socialism, and convincing evidence of growth retardation is provided by the experience of such countries as Great Britain under the labor government and France in recent decades.

Nations that have continued state ownership and control of all wealth, natural resources and capital equipment as well as current production, have survived only by the imposition of rigid controls in the hands of ruthless dictatorship. By such means socialism (of a kind) has been made to work and, at least for a few decades, to provide a growing economy. Such growth never has been great enough to compare favorably with that of nations having relatively free economies, although in some aspects of industry rapid growth may have been forced.[7]

Many people may believe that the gap between a relatively free economy and a controlled economy can be bridged as by the dashed straight line connecting the two points on the chart above the zero line. However, such never seems to have been the case. As an economy has become more socialistic while attempting to preserve political freedoms, the rate of growth has lessened and has become negative when complete socialism was approached. Then the inevitable inefficiency of a bureaucracy lacking ruthless power becomes evident. In order to restore a positive rate of growth (that is, in order to survive) such an economy has two choices: 1, to struggle back toward its lost freedom, as England has attempted to do under its present government (returning factories to private ownership etc.); or 2, to adopt more and more stringent controls until finally the reins of power are concentrated in the hands of a dictator (individual or small group). Whether or not a nation can struggle back from the economic morass of nearly complete socialism to the status of a relatively free economy remains to be seen. England may or may not provide the answer in due course.

Of vital importance in connection with our Nation's objectives are the following:

a. Continuing on the road to socialism will *not* maintain American economic growth at an annual rate in excess of Russia's; that path is *not* the dashed line on the chart, but the solid line that goes down to a negative rate of growth, to economic deterioration in fact.

---

[7]Some observers seem to believe that Sweden has proved that a democracy can adopt socialism successfully. However, in the first place Sweden is only partially socialistic, and emphasis has been placed on government control or ownership of natural resources rather than on the nationalizing of industry generally. (Even the basic steel industry was *not* nationalized as it was in Great Britain.) Second, the following figures on industrial production since 1950 (the year when West Germany regained its prewar rate of output) are of interest: increase in industrial production, 1950 to 1955, in Sweden, 15 percent; in West Germany, 79 percent; in Western Europe, 41 percent.

b. If we continue into the morass of socialism and attempt to "control" inflation by price controls and a broadening multitude of other controls that soon would seem necessary, we shall experience economic retrogression for years and at best succeed eventually in recovering to Russia's rate of growth (after prolonged delays) only by adopting a ruthless dictatorship thereby possibly achieving survival at the cost of much that, to many Americans at least, makes survival worth striving for.

In this connection we should also realize that once the absolute power implied in multitudinous centralized controls is permitted to exist, seizing of that power by a ruthless dictatorship will follow as night follows day. Such has been the invariable experience of mankind from ancient Greece to modern Russia or for that matter to modern America where concentration of nearly absolute power in some labor unions has brought to the top of those unions ruthless individuals from the gangster stratum of our society. That "power corrupts and absolute power corrupts absolutely" is but a half truth; the further truth is that where power is absolute, only the most alert, clever opportunist who is also utterly ruthless in grasping for power can hope to survive. By a process as inevitable in its outcome as evolution itself, only the "fittest" can survive and the "fittest" in such circumstances usually is the most brutal enemy of his fellow citizens.

The Route Toward the Nation's Objectives

That maintenance of an adequate national defense is essential for survival is obvious. However, defense in the long run involves more than preparedness for military operations; it also involves the continuing development of scientists, of science and technology, and of a growing industrial power capable of producing the unknown weapons of an unpredictable future.

The Nation's defense expenditures alone already are so great that the taxes providing the funds constitute a burden tending to retard industrial growth and hamper education of the Nation's youth. The financial problems of fathers attempting to educate their children require no emphasis for the hundreds of thousands in the moderate-income group who must pay income taxes in many instances exceeding the cost of the children's education. As for the young man earning his own way through college, if he succeeds in earning $1,500, hardly enough for a year in most colleges, the Government will take from him 10 percent of his income under present tax rates.

That existing taxes retard industrial growth is readily seen by anyone who understands that complex process called economic growth. Many people apparently believe that economic growth of an economy is achieved by a simultaneous general expansion of nearly all business elements within

the area concerned, such as a region or nation. Actually, however, that is *not* the situation. Economic growth is achieved, if and where it is achieved, as some elements of the economy expand more rapidly than those that are static or are contracting and perhaps are in the process of dissolution.

A striking example of a rapidly expanding segment of the economy was provided by the automobile industry through the 1920's. During the same period the carriage industry and to a lesser extent the motorcycle and bicycle industries were contracting. A small city not far from where this is being written was then known as the "whip city of the world." Today few youngsters in that city have ever seen a "buggy" whip, although many of the older citizens still remember the Sears two-cylinder "buggy" complete with dashboard and whipsocket, a memorial to the day when few believed the automobile could ever replace the horse.

Many factors other than obsolescence of the product account for the decline of business enterprises. These other factors include what may be called entrepreneurial arteriosclerosis (too much deadwood at the top) and numerous other forms of inadequate managerial ability as well as all the many reasons for personal and corporate failure including fires, floods, and earthquakes.

The vital point is that an economy can grow only when the increases in production of goods and services by the growing businesses exceed the decreases in production by the declining and failing businesses. Moreover, the most important function of profits in a competitive economy is to provide *both* the incentive *and the funds* for business growth, whether it be, at one extreme, the small business started by one man in its early stages or, at the other extreme, the huge corporate enterprise that has served the public for many decades. In short, profits are the food for growth, and whatever the corporate income tax takes must lessen the means available to business for expansion. Without doubt, today's corporate tax is a *most serious* inhibitor of business growth. Therefore, it retards development of the industrial power essential to maintain United States supremacy in a hostile world.

Obviously, the Nation's economic growth can be most rapid when *all* of the profits obtained in free competitive markets by businesses generally (excluding, of course, monopoly gains and other profits attributable to special privilege) are left in the hands of the businesses concerned. Whether the profits are directly invested in new plant and equipment for expansion or in part are paid out as dividends (thereby attracting more capital to the industry) is a relatively unimportant operating detail.

Moreover, taxes on profits can kill overall economic growth if the

discouragement to growing enterprises slows their growth enough so that it is equaled or exceeded by the decreases in production of obsolescent and failing enterprises. Perhaps the tax on corporate profits already is so high that aggregate growth will be prevented in the absence of such a great and dangerous inflationary stimulus as that of the past decade. If such is the situation, the Nation already is seriously jeopardized.

These considerations point to the following route toward the Nation's objectives.

1. Defense expenditures must be kept at the minimum consistent with adequate defense by strict economy, elimination of duplication, etc. For example, are separate postgraduate "colleges" for senior officers of the three armed services plus a fourth National War College, all with various duplicating courses, really essential? Are mobile missile bases, on railroad cars and trailer trucks, more effective and less costly than the elaborate missile bases now under construction? The locations of the latter inevitably will be known to the enemy, whereas mobile bases would be indistinguishable among millions of other vehicles and thus nearly as well-concealed as are submarines in comparison with aircraft carriers.

2. All unnecessary Government expenditures should be eliminated, especially those interfering directly with achievement of the Nation's objectives.

3. Expenditures for aid abroad should be reduced to those *clearly and directly* in support of our national objectives.

4. The following principles should be applied in reducing and readjusting the Federal tax burden:

a. Taxes on business profits, except profits attributable to monopoly and other special privileges, should be *reduced rapidly and eliminated as soon as possible* in order to encourage economic growth to the maximum extent.

b. Because of the great and obvious need for more and better education for the Nation's youth, college tuition and other necessary expenses should be allowed as deductions from family incomes before taxes.[8]

c. As rapidly and extensively as possible personal taxes should be shifted from *earned* incomes to incomes derived from special privilege

[8]Consideration might also be given to putting *all* estate and gift tax receipts into a special fund distributed to all accredited colleges for scholarships. Such an arrangement (using already existing and least costly administrative facilities) would help in achieving that national objective, *equality of opportunity* for all. In effect, some of the States now follow this procedure with their share of such taxes through their support of State universities open to all qualified applicants at minimum tuition.

of every form and variety. In this connection three important distinctions, wherever feasible, should be made.

(1) There is no important economic reason why tax rates on special privileges (including site monopolies, etc.) should not rapidly approach 100 percent of income after certain basic personal exemptions.

(2) Taxes on interest and dividends from capital invested in competitive enterprises (as distinguished from funds used to buy monopoly privileges) should be kept as low as possible in order to avoid inhibiting investments in such enterprises.

(3) Taxes on *earned* incomes should be eliminated or reduced to the lowest possible levels, especially where the earnings are from potentially growing but small individual enterprises.

To some readers these recommendations may seem unrealistic counsels of perfection without hope of practical application. Three objections probably will be offered, viz:

1. That the great mass of the voters are "too damn dumb to understand."

2. That the pressure groups, for example the farmers, are too strong.

3. And, during any period of recession, that we must do something to restore prosperity promptly at all costs because, as the witty Lord Keynes put it, "In the long run we are all dead."

There are two effective answers to the first objection. Too many people, including historians who should know better, seem to have forgotten that in the depths of one of the Nation's worst depressions, in 1932, the American people chose as President *not* a "pied piper" who promised to restore prosperity by spendthrift magic but a man who promised over and over *to reduce Government expenditures by 25 percent,* who deplored in the strongest terms Washington meddling with and direction of the economy, and who, during the first months in office, actually pressed Congress for reductions in spending. The New Deal spend-for-prosperity notions came later; and, if the public apparently did approve them in 1936, that presumably was because of the delusive business improvement at that time and the claims "we planned it that way" broadcast before the elections. Subsequently, the 1937-38 depression, one of the most rapid and extensive declines in the Nation's history, dispelled the earlier illusions of success in restoring prosperity.[9]

---

[9]Those who would cope with depression by increased Government spending might well reflect on the fact, mentioned earlier in this chapter, that there were still nearly 10,000,000 unemployed in 1939, a full 5 years after the New Deal spending program began, and that even during the abortive recovery of 1936-37 nearly 8,000,000 were unemployed.

The second answer to the first objection is that a relatively small group of the better informed independent voters, even those who are registered Democrats or Republicans, hold the balance of power in most elections. Once the politicians sense that this group has decided views on any question, those views will be reflected in political action. If sound economic analyses are made available to and are accepted by the Nation's more thoughtful and independent voters, the conclusions of such analyses may become the guide to action.

With reference to the second objection, that the pressure groups are too powerful, the fact is that a decisive majority of the farmers responding to a recent poll *disapproved* of the Government's efforts to support prices of agricultural products. Half of those replying wanted no Government aid in any form. There simply is no evidence convincing to us that the Nation's farmers as a whole put their personal welfare ahead of the Nation's.

As for the third objection, that "in the long run we are all dead," one cannot deny the truth of this assertion, but one can deny its apparent significance as an argument for more inflation to restore prosperity. The fact is that our children and grandchildren will be alive in the long run unless we continue to mismanage the Nation's economic affairs as we have during our lifetimes and leave for our descendants a nation vulnerable to Russia's attack. In short, if the Nation is to survive, we must focus our attention on what is wise in the long run and struggle as best we can to cope with the difficulties of the short run.

This does not imply that the unemployed should be permitted to starve nor that all in debt beyond their immediate ability to pay should be forced into bankruptcy and should lose their homes or other possessions; but it does imply that the gross distortions within the economy should be corrected by the sometimes painful processes of freely competitive markets rather than be augmented by still more inflation with even more unfortunate future results.

It implies also that the deterioration of the Nation's educational system should cease, and the relative economic status of educators should be improved, even at the cost of ending the monopoly powers of unions as well as those of industry; moreover, means should be provided to move toward equality of opportunity for youths capable of benefiting from higher education. We should never forget the lesson of long experience: that deterioration of the Nation's schools tends to parallel depreciation of the dollar simply because inflation results in adverse selection of educators by tending to shift the more competent to other jobs and by attracting the least competent to fill the vacancies.

Sound comparative analyses should be substituted for the grandiose dreams of recent years; we should face the fact that resources are

limited and put first things first by weeding out programs that hinder progress toward the Nation's objectives and by reducing expenditures on programs having a relatively low priority in comparison with the Nation's need for economic growth and maximum educational opportunities.

The science of economics is relatively immature. Much that is published on the subject, including supposed remedies for recessions, has no more scientific standing than the notions of the itinerant medicine men who sold health elixirs to a gullible public a few decades ago. More specifically:

a. Confidence is not a satisfactory substitute for the correction of serious maladjustments in the economy; in fact, confidence insofar as it invites complacency and a "stand pat" attitude can delay recovery by postponing needed readjustments in prices, wages, etc.

b. "Pump priming" by means of large government expenditures never has resulted in a sound, stable, and lasting recovery from depression.

c. Contrary to the implications of those who recommend perpetual inflation and rising prices as the road to prosperity, rising prices are not essential to prosperity. The record shows that the most rapid and best sustained economic growth in the Nation's history occurred from 1875 to 1892, when prices were declining almost steadily and by the end of the period had decreased 35 percent.

Of course, the basic requirements of American citizens at this time are willingness to face the facts, to learn the lessons of costly experience, and determination to follow the route to national survival regardless of whatever personal inconvenience may be involved. One function of the Institute is to analyze facts and publish the economic lessons thus provided. Determining that a sound course will be followed and urging that course on the Nation's legislators are the tasks of every American citizen who chooses to do his duty in the Nation's hour of need. Unless these things are done, we shall not only pass along to our sons and grandsons the mess that we have made in recent decades, but also we shall betray them finally by destroying that one great hope for the future of mankind, the basic principles of a free and just society embodied in the Constitution of the United States.

II.

LEARNING FROM EXPERIENCE

The United States Stands Alone

Nearly two centuries ago an embryo nation of a little more than 3,000,000 population occupied part of the eastern coastal area extending from southern Maine to northeastern Georgia. All but 10 percent of the people lived in small villages and remote clearings connected (one might better say *separated*) by trails that for the most part were passable only for men on foot or horseback. Only 6 cities had populations exceeding 8,000; and the largest, Philadelphia, numbered only 42,000.

The industrial revolution had hardly reached this side of the Atlantic. The first cotton mill in North America had not then been established, and other industries were in the primitive handicraft stage. For most manufactured goods the people were dependent in large part on imports from England or the other developing industrial nations of Europe.

To the north of this nation-in-embryo was Canada, colony of the great European power from which independence had just been won. In the south and southwest a vast area, including what is now Florida and much of the great Mississippi Valley, was held by Spain, a second great European power. Within a few years Napoleon, Emperor of still another European power, was to claim the great Mississippi area for France. Compared with those giants of the times, the embryo nation was but a pygmy about equal in population to the smaller nations of Europe.

In the remote villages and wilderness clearings men went to their work in the fields equipped with muskets, prepared to repel Indian attacks. The inhabitants of the cities, which were all on the coast or on navigable rivers near the sea, well knew that at any time their homes might be burned to the ground by hostile sea-born forces; and threats of such assault were not infrequent. As disputes flared up with first one then another of the European powers that had a foothold in North America, one could never know when a monarch's dreams of conquest would incline him to order his fleet to burn and pillage on the coast of the New World. Almost as though to emphasize that fears of such action were justified, the capital city of the infant nation was burned by British marines before three decades had elapsed.

Nevertheless, the people of this embryo nation somehow found the courage to stand alone. Instead of seeking an arrangement whereby the

ruler of one of the three great European powers might have become their Emperor and protector, the inhabitants resolved to create a new society in the family of nations. A Constitution was formulated, finally adopted, and the United States was born.

The objectives of the new nation as outlined specifically and implicitly in its Constitution were revolutionary in the sense that they visualized and provided for overturning the old and establishing the new in the affairs of mankind. The citizens of the new society were to be equally subject to the law and were to cooperate voluntarily by means of free competition with special privilege for none and equality of opportunity for all. With those objectives so clearly sculptured in the very foundation stone of the new society the United States stood alone in a largely hostile world, a world organized far differently and with greatly different objectives.

How stands the former infant nation among the great industrial powers of today? To the new small nation of two centuries ago the industrial revolution came in due course, and progress at a rate not elsewhere equaled was the fruit of relatively free enterprise. Countless individuals were stimulated by relativly free competition, were financially strengthened by being permitted to reap where they had sown, and were encouraged by unlimited opportunity to do on a larger and larger scale that which they could do best for society. From their talents, in some instances bordering on genius, innumerable businesses, even whole industries grew. John Fitch, Robert Fulton, Eli Whitney, Peter Cooper, Phineas Davis, Francis Lowell, John Goulding, Cyrus McCormick, Charles Pillsbury, Gustavus Swift, Andrew Carnegie, Thomas Edison, Henry Ford; these were but a few of those whose talents were reflected in the vast growth of industry in the United States.

The result has been that the United States today is the industrial leader of the world. The total capacity of the United States steel industry is 148,000,000 tons annually, about 40 percent of the steel production for the entire world; our capacity is about double that of England, France, and Germany combined and is 2½ times that of Russia. The *increase alone* in American steel capacity since World War II began roughly equals Russia's *total* output in 1960.

With reference to numerous other products of a modern industrial nation the story is much the same. Although including only a little more than 6 percent of the world's population, the United States produces and consumes nearly two-thirds of the world's aluminum, about two-thirds of the motor vehicles produced in the world, about 40 percent of the electric energy (nearly 4 times that of Russia); and it has two-thirds of all the world's telephones in use.

Yet there are those who assert that we dare not stand alone in a

possibly hostile world; that we must have friends to help protect us from potential enemies; that we must outbid Russia in the search for allies; that we must support governments abroad determined to impose on their citizens procedures and objectives alien to our own and conflicting with our form of society. Although we know, if we have learned anything from our own experience, that the road to socialism is the road to ruin, we are told that foreign governments "hell-bent" for socialism must be supported by taxes levied on our citizens, all because some assert that we dare not stand alone.

Isn't it long past the time to face the fact that the United States still stands alone as it has for nearly two centuries? Except for a few small nations, relatively inconsequential measured by industrial might, no other nations are with the United States in pursuit of the same basic objectives.

Consider England, for example, with whom we probably have more in common than any other large nation. True, England is a freedom-loving democracy in the popular meaning of that rather vague phrase, but England's objectives are not the same as ours. England is still a nation divided, in large part, between a landed aristocracy and other custodians of great wealth on the one hand and on the other hand a multitudinous and largely disinherited proletariat.[1] When the financial and other vested interests of Great Britain and the remnants of the empire are threatened by such an event as Egypt's seizure of the Suez Canal, the governing group not only has no hesitation in sending the common citizen to war but also the government does not even bother to consult the people about the matter. (That the government also neglected to keep its supposed ally informed, the ally who was paying some of the bills, was only what we should have expected had we stopped to reflect on the differences between England's objectives and our own.)

Then consider France. Once there was hope that the objectives of the United States would become the objectives of France, but that was nearly two centuries ago when the French Revolution first began. Lacking a foundation as stable as our Constitution, that unfortunate nation soon reverted to a monarchical form of government, crowned Napoleon emperor, and since has regained only the semblance of a free-enterprise republic. Special privilege exerts an influence in government such that

[1]England has a more numerous middle class than have most European nations, but this element of the population in recent decades has become politically impotent. When in power, the Labor Party has turned to socialism as a means of taking capital and income from the aristocracy of wealth in the hope of effecting a different distribution of income. Ground between the millstones of Socialist taxation and inflation, the middle class has experienced drastic deterioration of its economic status. Of course, the aristocracy of great wealth, although subject to high income and estate taxes as long as they remained vulnerable within Great Britain, have transferred holdings to relatively tax-free Bermuda, the West Indies, and elsewhere. Also, and especially in the absence of a capital-gains tax, the wealthy readily have found ways to profit from the continued inflation.

apparently interminable war has been chosen in order to protect French vested interests in North Africa. The French Government joined Britain in the ill-fated attack on Egypt, also without consulting either its own citizens or the United States.

Does any sensible man really expect France to prove a stouthearted ally if Russia attacks, regardless of how much money and equipment we give to France? Inasmuch as France capitulated at the threat of German bombing of Paris in 1940 (with ordinary bombs) when her own existence as a nation was involved, why should we expect France to brave the threat of nuclear bombs from Russia in order to assist the United States?

The fact is that Europe, with minor exceptions, is an aggregation of countries where special privilege long has held the reins of power. The disinherited proletariat has found but two principal ways of coping with the situation: 1, to emigrate to the New World; or 2, to impose socialism at home in a misguided effort to obtain "fair shares." If the more numerous underprivileged of those nations ever have entertained the notion that our objectives should be theirs, they have not yet displayed competence to effect the change.

As for the landed aristocracy and in the present age the equally or more numerous beneficiaries and guardians of great corporate wealth, their privileges have been held so long as to seem like natural rights. They have no more intention of giving up their stranglehold maintained by means of land monopoly and international cartel arrangements than a tiger would have of giving up her cubs. To those powerful interests, the American dream of a better society seems like a foolish dream indeed, and they would not hesitate to use their counterparts and financial allies in our own Nation to defeat progress toward our objectives if that progress seemed to endanger their power and privilege. Many United States citizens and many more of the parents of present citizens came to this country from Europe in order to escape from the situation that there prevailed and for the most part still prevails. Taxing them now to support the conditions from which they fled hardly seems a worthwhile project. Would not the funds be better used here in furtherance of their and our objectives or, if used abroad, used in support of those same objectives elsewhere?

Parenthetically, we should make clear at this point that we do not imply that the United States should turn a cold shoulder to England, France, and other possible allies. Wisdom dictates that even such allies as Spain be sought if the end result is to the best advantage of the United States. However, in cooperating with other nations wherein and to the extent that our mutual interests coincide, we should avoid the sloppy sentimentalism that is blind to many significant facts in the situation. At least, we should avoid strengthening the hands of Socialist

governments whose ultimate "success" must ruin our erstwhile friends. Moreover, not a dollar should be given or loaned abroad unless sound comparative analyses indicate that such use will accomplish more toward achieving United States objectives than could be expected by either using that dollar at home or leaving it in the pockets of the citizens from whom it must otherwise come.

As for many other nations of the world that have been the recipients of our lavish gifts and "loans" in recent years, most are either absolute monarchies, military dictatorships, or oligarchies under the control of powerful landholders or other privileged groups. Some of our aid has served only to make the rich richer, to put more Cadillacs in families where there was only one before. In other instances we are attempting to aid impoverished and backward peoples without sufficient analysis of the reasons for their ages-long condition and therefore without an adequate basis for believing that our aid will be effective in the long run.

Of course, this liberal distribution of largess and advice reflects two aspects of our own misconceptions: 1, the delusions of economic grandeur that always have accompanied our periods of prolonged inflation; and, 2, a singular overconfidence in our ability to prescribe how prosperity may be attained by others in view of our obvious inability to preserve it for ourselves.

In the meantime, what have we done at home in recent years? We have engineered the greatest inflation in the Nation's history; we have induced millions of our citizens to incur debts for homes, cars, etc., in the belief that ever-increasing prosperity would be or could be made permanent; we have robbed holders of life insurance, savings, etc., of nearly $200,000,000,000 in the short space of 20 years; we have encouraged a widespread and fatuously complacent overconfidence in the Nation's future while failing even to see the basic problems that must be solved if United States objectives are to be attained.

Now the time has come when continuing to avoid facing facts may be disastrous. If we ask the right questions, we may in time find the right answers and thus progress toward our objectives. When and if we do that, we shall be in a position to invite the rest of the world to follow, if they choose to leave the swamps of socialism and the deserts of despotism. In the meantime, we should remember that we still stand alone and must continue to stand alone unless we choose to abandon pursuit of those national objectives that make the United States the only hope for a despairing world.

Asking the Right Questions

Solutions to the problems of men are found, when they are found, by first asking the right questions. Today we in the United States are

confronted with three problems of critical importance: 1, boom and recession; 2, apparent departure from, rather than the desired approach to, the Nation's basic objectives; and 3, survival in a hostile world. How shall we ascertain what questions to ask, and how may we find useful answers?

Once upon a time men sought solutions to their problems by asking questions such as: What one or more of the Gods have I offended? How may I appease them? Who among our medicine men possesses the most potent magic and can best intercede for me? Here in the United States, at least, we have long since learned that these are not the right questions.

Not quite so outmoded are questions of a somewhat different type such as: Where in our folklore shall I find the answer, or Who among the wise men can tell me the proverb that suggests a solution to my problem? But we of Western civilization no longer expect to find in proverbs handed down from antiquity the solutions to all current problems in this age so influenced by the development of modern science. In the days when most proverbs summarized the common sense of the times, many of today's complex problems simply did not exist.

And at other times and places men have sought the advice of philosophers, have asked them, What is the Truth, the absolutely certain, guaranteed, and everlastingly correct answer to my problem? Philosophers of two general varieties, the Platonic idealists and the Aristotelian logicians, both offered answers for the questions of men, unfortunately not with unqualified success.

Then finally a few men happened upon a different method of conducting inquiries. They put aside the spooks and fairies, demoted the mythical gods and goddesses, discounted the folklore and superstition embodied in proverbs and old wives' tales, abandoned the quest for certainty, and instead asked questions such as these: What measurable changes occur and what uniformities of relationships are found among those changes? What actual sequences do we find in the natural world of things or events? What hypothesis or theoretical explanation is suggested by the facts and can be adequately tested by a check of the necessary implications of the theory? Can it be used for successful prediction and control over the future facts or our adaptation to them? Such questions proved to be "right" in the sense that the answers, when found, have been useful in coping with the problems of men.

The successful method of inquiry now generally called scientific was first applied to certain physical problems of men. To the question, does the earth revolve or does the sun move around the earth, a useful answer was found by the methods of science. True, some of the pioneers who thus sought answers were tortured by rack and screw,

and the answers that they found were not generally accepted for many decades; but, in the long run, these answers prevailed.

Similarly with the physiological problems of men, the pioneers of modern medicine were scorned by most professional teachers and students in the field. The conclusions of Vesalius and of Harvey were accepted only after prolonged debate; in fact, some of the pioneers even were cast out of their professional groups and died in poverty because they espoused new ideas.

Less personal sacrifice has been involved for those who are leading the scientific advance, the revolution in methods of inquiry, in the behavorial fields, especially in economics. However, there is every present indication that the battle to establish scientific methods of inquiry will last for decades even if it is not so bitter as were the earlier battles in the physical and physiological sciences.

Although scientific methods of inquiry have been well under way on an organized basis for nearly four decades in the social sciences, following the earlier efforts of a few pioneers, many economists still cling to the older methods of inquiry. The Keynesian spend-for-prosperity notions taught in many colleges provide an excellent example of the cultural lag with their foundation resting on secular revelation and their web of theories spun from introspection, casual observation, and vivid imagination in the best scholastic tradition of the dialectical quest for certainty. As a result we find even in one of the Nation's leading technical institutions an economics professor teaching sophomores that perpetual inflation with an increase of 5 percent annually in prices (that is, depreciating the dollar at this rate) is desirable;[1] and in a nearby university an eminent economics professor also advocated perpetual inflation (his suggested annual rate of depreciating the dollar being 3 percent).

Another school of economists, typified by Hayek and Von Mises, although their methods are similiar to those used by the Keynesians, arrive at diametrically opposed conclusions. Yet neither the Keynesians nor the others have as yet grasped the obvious fact that the answers they provide are suspect because of unsound, in the sense of proved-to-be-inadequate, methods of inquiry. In fact, only because the method they use is unsound is it possible for men of otherwise good intellects to derive such conflicting answers.[2]

---

[1]For a more extensive analysis of Professor Samuelson's teachings at the Massachusetts Institute of Technology see the review of his book *Economics, An Introductory Analysis,* in E. C. Harwood, *Reconstruction of Economics,* American Institute for Economic Research, second edition, 1960, pp. 23 to 32. (In the fourth edition of his book Dr. Samuelson changed his approved rate of "creeping inflation" to 2 percent annually, without giving any reasons for the change from his original 5 percent.)

[2]For a more adequate discussion of this situation see the reference cited in footnote 1, pages 7-22, 73-82, and 99-103.

Parenthetically, of interest is the fact that application of modern scientific method in the general field of sociology (or what might be called a combination of sociology and anthropology) appears to be on the verge of a major breakthrough comparable to Galileo's successes in astronomy more than three centuries ago. Leaders in this field now believe that they have scientific proof of the survival value of individual freedom and equality of opportunity in a human society.

We turn to some of the questions that should be asked in relation to each of the three major problems indicated at the beginning of this chapter.

Concerning any future recession, we should ask:

1. Has modern scientific method provided a tested explanation of the more extreme cyclical changes in business activity?

2. What are the implications of that explanation as far as alleviating or remedying the situation are concerned?

3. What should be done to minimize the extent of such developments in the future?

Fortunately, in large part through the work of the National Bureau of Economic Research and our own organization during the past four decades, the answer to the first question above is "yes." Some useful answers to the second question also have been developed. The general character of useful answers to the third question is apparent, but details remain to be worked out.

With reference to the second major problem, apparent departure from, rather than the desired approach to, the Nation's basic goals, answers to the following questions are needed:

1. To what extent and in what ways are departures from the basic goals measurable, even in a general way?

2. What are the explanations for the divergence of results from expectations?

3. What changes in statutes, customs, etc. can serve as a means of achieving the desired ends?

Although some work in the attempt to answer these questions has been done, much more remains.

Concerning the problem of survival in a hostile world, such questions as these should be asked:

1. What are the conditions precedent to optimum growth of a modern industrial nation?

2. How can the Nation develop to the maximum extent its resources of human intelligence in order that our lead in the scientific and technological advance may be maintained?

3. What is the relative importance (for survival) of more ex-

penditures for defense, various kinds of foreign aid, internal subsidies such as those to agriculture, aid to education, etc., etc.?

No one having any conception of the complexities involved would assume that the answers to all these questions can be found in less than several decades of comparative analyses requiring painstaking and continuous application of modern scientific method, although we need not wait long for many useful answers. The Institute has developed portions of some of the answers, but the scope of the problems is greater than our present sphere of activity.

As for how more of the answers to these questions may be found, we proposed a few years ago that an independent and nongovernmental advisory council for scientific inquiry into the problems of men in society was needed. Such an advisory council could develop, by modern scientific methods, useful answers to be made available to the public.

Experiences with temporary commissions of inquiry here and abroad have demonstrated that such devices are a logical and essential element of social organization in a republic or "democracy," as most republics are called today. However, for inquiry into problems that cannot be solved quickly, we believe that a permanent group is needed. With the aid of leading behavioral scientists, we have initiated such a council, one that is completely free of all ties to vested interests, political, business, or other.

If the work of the proposed advisory council is sound and if enough of the Nation's more independent voters (those who hold a balance of power in most parts of the Nation) choose to accept its findings and recommendations, there is reason to believe that such findings may become influential in legislative halls. We know of no better means by which useful solutions for the Nation's major problems may be developed and applied.

In a republic or a "democracy" the common sense of the citizens presumably provides the guide for legislation and custom. In matters physical, for example in bridge construction, the citizens of the United States have adopted as their common sense the findings of qualified scientists, not of course in full technical detail but as a guide to action; in matters physiological, for example, vaccination against smallpox, the views of qualified scientists similarly have been adopted as the common sense of the citizens. We believe that the warranted conclusions of qualified behavioral scientists must be made available for acceptance by citizens as a guide to action if our Nation is to survive. In short, we believe that twentieth century common sense should include the findings of qualified economic and other social scientists as rapidly as such scientists can be found or trained and warranted assertions can be developed by them.

What About the Unemployed?

Few members of a modern industrial society can avoid losses and, in some degree, hardship during a severe recession or depression. Thousands who have invested in businesses forced into bankruptcy lose their accumulated capital; millions who have invested in the securities of businesses that survive nevertheless lose if forced to sell during a depression, and their incomes are curtailed when dividends are reduced. Hundreds of thousands of business managers find their usual worries multiplied as they strive to find the funds to meet next week's payroll. All of these individuals deserve sympathy not only because of their plight but also because many of the panaceas usually urged upon or by Congress would hamper rather than encourage the efficient functioning of free markets whose decisions are needed in order to correct maladjustments and restore prosperity at the earliest possible date.

With reference to the unemployed, however, much more than sympathy is required. All citizens bear part of the responsibility for the situation of the unemployed, who are entitled at least to a livelihood for themselves and their families while the necessary readjustments are being made.

The responsibility of all citizens for the plight of the unemployed rests on two bases. In the first place, if more progress had been made toward the Nation's basic objectives, the unemployed as well as others presumably would be in a better position to cope with present difficulties. Second, who but the citizens as a whole should be held responsible for the great inflation since the beginning of World War II and the results of that prolonged inflation?

The fact is that the public, acting through both Democratic and Republican administrations of the Federal Government, put in motion and kept in motion the great inflation that stimulated the prolonged business boom, that cut short the minor interruptions in the postwar years, and that accounts for the extent of the distortions now requiring correction. Even the more prudent of those unemployed, who waited as long as they reasonably could before purchasing homes for growing families, found their attempts to be prudent penalized by the continually rising costs of new residences as organized labor in the building trades and elsewhere took advantage of the great inflation.

The unemployed as well as others may have incurred debt unwisely, may have undertaken too large a burden of monthly payments. Some would have been improvident in any event; but was not the continuing rise in prices more than an inducement, was it not an actual threat that if they did not incur debt they would continue to lose some of the buying power of any dollars they saved?

Moreover, who is responsible that the unemployed when receiving half or a third of their regular wages must still pay high prices for food that, in freely competitive markets, would be available for much less? The economic folly of subsidizing agricultural surpluses by maintaining artificially high prices becomes worse than mere folly in depression times; how should we characterize the actions of a government that deliberately raises the price of food when millions of its citizens are on a bare subsistence dole? Surely this is a strange procedure for a nation to adopt under the guise of promoting the general welfare.

Even continuation of the dole, of public relief, to say nothing of the more liberal unemployment compensation available to a portion of the unemployed, will be partly at their expense unless more inflation by the monetization of deficits is avoided. More inflation will push prices up further, will depreciate or lessen the buying power of the last reserves of the unemployed, the currency in the pantry sugar bowl, the last life insurance policy, perhaps a few U. S. savings bonds, or a savings deposit. Thus to the obvious robbing of Peter to bribe Paul via taxes to support prices of food at unnecessarily high levels will be added the subtle embezzlement effected by a depreciating dollar.

In fact, the very process of paying people who are not producing tends to result in more inflation. Dollars thus go chasing goods without a corresponding addition to the supply of goods in the markets. Unless care is taken to raise taxes or to borrow from the current savings of those whose incomes do represent production, (that is, unless further monetization of Federal deficits is avoided), the more the doles or the relief and unemployment payments, the less each dollar of them will buy in the markets.

Reabsorption of the unemployed into the production processes as rapidly as possible is the objective. What can be done to expedite progress in that direction?

The situation in the automobile industry offers a case in point. During years of prolonged inflationary prosperity the principal companies found increasing profits readily obtainable. Organized labor was alert to the possibilities and demanded a share of the windfall profits. Corporate managers acquiesced, perhaps because they saw no other way or perhaps because they simply concluded that continuing inflation would enable them to keep one jump ahead of labor's demands. Be that as it may have been, the net result has been a quadrupling of automobile labor's average weekly wage (including fringe benefits) since 1939.

The automobile industry is not the only segment of the economy where wages have more than quadrupled, but in several important segments the increases have been much less, and in some segments the increases in wages have not even compensated for the rise in the cost

of living. For example, wages of employees in the entire educational system of the Nation, from kindergartens through the university graduate schools, have lagged far behind. Even full professors in most of the Nation's colleges today receive little more than many steel workers or automobile workers earn including their overtime pay. Below the grade of full professor and down through the public schools, most teachers of the Nation's youth are less well off today than they were in 1939.

In any event, the principal point to be made here is that some segments of the population that have derived most advantage from the great inflation now have priced themselves out of much of their former markets. In the absence of more and more inflation, how can some segments of the economy hope to maintain their seriously unbalanced position in relation to the rest of the population?

With these facts in mind, we offer a suggestion. In order to outline it definitely we use specific figures, but the principles involved rather than the illustrative figures are important.

During a recession, for example, General Motors might say to their employees something like this:

1. Obviously, our employees, the stockholders, and we, the management, have profited greatly from and during the prolonged inflation of the postwar years. Equally obvious is the fact that our product cannot be sold in the volume we should prefer at today's prices. Many of our former employees have no wages, and most of our present employees are earning less then they were, management's bonuses will decrease, and dividends will be reduced or cease unless we can alter the situation.

2. Profits have been reduced 100 (or whatever) percent from the peak levels of recent years.

3. We propose a *temporary* reduction in *all* wage rates and salaries of *half* the percentage reduction in profits, plus a bonus with the following understanding:

a. The company will resume production at what is believed to be the most efficient rate of operations, rehiring as many as practicable of the capable, former employees.

b. Simultaneously, prices of cars and other products will be reduced to what the management believes will be a break-even level with normal production for a 40-hour week. Prices may be adjusted upward if the resulting demand proves to be even more elastic (responsive to lower prices) than the demand for cars always has been.

c. Shortly after the end of each quarter, any profits obtained will be shared with employees as an incentive bonus or supplementary wage so that when net profits, after deducting taxes and the supplementary wages, have recovered to half those of the last peak year the supple-

mentary wage payments will restore half the cut in wages (bringing wages to 75 percent when profits are at 50 percent of former peak levels); when profits have recovered to 80 percent, supplementary wage payments will restore 80 percent of the cut in wages (bringing wages to 90 percent of peak levels), and so on. (Dividends to stockholders presumably would be in proportion to the net profits remaining for the company.) It is further understood that a final adjustment will be made annually and that when and if net profits again reach the last peak levels, the wage and salary scales shall be fully restored and employees shall be free to bargain and strike for higher wages or whatever arrangements they prefer. The accounting aspects involved may be checked by independent auditors.

Perhaps we should add that we at the Institute are not so naive as to expect such a plan to be welcomed at first consideration either by General Motors or by organized labor. However, there is nothing like a depression for stimulating the exercise of ingenuity.

In effect both labor and management, if such a plan were adopted, would simply be taking advantage of the lesson to be learned from free, competitive markets. One can, of course, learn the hard way, by prolonging unemployment, forcing great losses on the company, possibly bankrupting the union, and in general being as shortsighted as organized labor and management were in England after World War I, for example. However, we see no inherent necessity for such stupidity.

How long a period would be required for wages and profits in such maladjusted industries to recover to former peak levels, no one can foresee. Given renewed opportunity for balanced growth, recovery to and extension beyond former peak levels might occur in a surprisingly short period of a few years.

When conditions seemed darkest in the spring of 1933, President Roosevelt inspired some people by his confident assertion that we had "nothing to fear but fear itself." Heartening as this message may have been to many listeners, subsequent events proved that the Nation had much more to fear than fear itself. What should have been feared far more was that men of unquestioned good intent would be governed by their hearts rather than by wiser heads, that good intentions would pave a six-year-long road through the "hell" of unemployment for those who already had endured such hardship too long. Good intentions are not enough. Good intentions play a vital part in providing the urge to act, but impulsive action aimed at alleviation of symptoms rarely remedies serious economic or other maladjustments. Now we can avoid burdening the unemployed with a decade of frustration and heartaches if we apply the lessons of past experience, lessons that should be part of our common sense.

III.

THE COUNTERREVOLUTION

The struggle against communism is not an attempt either to destroy Russia or to preserve the United States; it is not merely another of the numerous rivalries between nations that have crowded the pages of history. The struggle against communism is a crucial one for the survival of Western civilization. Whether this struggle will mark the decline and fall of Western civilization or will set the stage for a new, great advance comparable to that of recent centuries remains to be seen.

Because this is not merely a struggle between jealous or greedy monarchs nor solely a war for empire and trade nor a religious war between ignorant and intolerant tribesmen, we must seek below the surface and behind events of the day for the fundamental causes of the conflict within Western civilization. At least briefly we must sketch the outline of developments on a broad front and in the perspective of recent centuries.

Several hundred years ago Western civilization consisted of many vast feudal estates, innumerable peasant holdings of small farms, uncounted villages and towns, and a few cities, small by today's standards. For the most part, men lived as their fathers and grandfathers before them had lived; folklore and superstition were generally considered the intellectual keys to understanding, and scientific knowledge as we think of it today was almost unheard of; class distinctions were rigid in many parts of the civilized world; village industry was controlled by the guilds and other authorities; progress was not generally expected and often was not tolerated; most men were slaves, seemingly held in perpetual bondage by custom, fear, ignorance, and superstition.

Nevertheless, within that civilization an idea began to find increasing acceptance. In a word, this was the idea that individuals might be *free;* but its scope developed gradually, and even today we are not sure that we grasp its full implications.[1]

Aided by many circumstances that need not be described in detail,

[1]In summarizing our Nation's objectives on pages 10 and 11, we suggested that men are free to the extent that the culture or society in which they live permits them to plan and choose their goals, provides equality of opportunity to act effectively in pursuit of those goals, and permits them to retain the fruits of their labors. Throughout this report we shall use the word *freedom* as a blanket label for these circumstances and such others as may be necessary to constitute optimum conditions for the economic welfare of men in society. We realize that such use of a term is loose characterization rather than scientifically accurate specification or naming, but it will serve the purpose here.

this idea of freedom found more and more disciples. It attributed worth and dignity to the individual man; and, as men gradually and almost reluctantly accepted this new idea, they likewise accepted many increased responsibilities that fostered individual growth in countless ways.

Intellectual freedom opened new frontiers of science. As a result, technological progress rose like a giant from sleep to aid the wealth-producing activities of men. Here in America circumstances were most propitious for a civilization based on the idea of freedom. The results we are familiar with; but the magnitude of them is sometimes overlooked, because to us they have become commonplace.

Freedom found acceptance in parts of Europe also. Major social changes marked its advent, and great material progress was one result. However, in much of that area this great revolution never was so successful as it was in the United States. Apparently in only two countries of Europe, Denmark and Switzerland, has the great revolution maintained its gains or progressed in recent decades.

Even here in the United States, however, complete freedom was not reached. Conditions here differed greatly in many respects from those in the Old World; but we now realize that various laws and customs that were carried over from the Old World had the effect of denying freedom, at least in some degree, to many of the people of our own Nation.

The results of imperfect or partial freedom were also imperfect. Great material progress came, but the greatly increased production of wealth was not equitably distributed to those who produced it. As a result, 12- and 14-hour days for women and children were common in the factories of England, more extensive and more degrading poverty pervaded the slums of Europe, and urban and rural slums developed in the United States.

So striking did the increasing maldistribution of wealth become that many men abandoned the battle for freedom and turned back; thus the counterrevolution within Western civilization was born. For the past hundred years the counterrevolution has been gaining strength. Its basic ideas were developed earlier by the Utopian Socialists and were organized as counterrevolutionary doctrine by Karl Marx and his followers. These ideas are the roots from which modern communism, socialism, fascism, the New Deal, and the welfare state all have grown.

In Russia the counterrevolution has reached the apparently inevitable goal; a new despotism has replaced the old. In this fact there is a lesson for all who desire to learn it. Marx and Engels predicted success for communism (the militant branch of socialism) first in the great industrialized nations where they expected the proletariat to unite and cast off its chains. But communism succeeded first, not in the more advanced industrial nations, but in Russia, where the progress of the great revolu-

tion had been retarded. The reason is not difficult to understand. The counterrevolution is fundamentally a retreat from individual freedom, from responsibility and authority for each individual, to the sheltering arms of an all-powerful state. Naturally, communism succeeded first where the progress of the great revolution had been least; and it still achieves success most readily in the backward nations of the world, where the substitution of a new despotism for the old is relatively easy.

The Source of Communism's Strength

The fact that communism succeeded first in Russia and that it gains ground most rapidly in the more backward nations of the world should not be permitted to encourage a false sense of security. The basic principles of communism have been widely accepted; and the counterrevolution has gained strength during the past century in nearly all nations of Western civilization, including our own. In order to grasp the significance of these gains, we must first understand the source of the strength of communism.

Although the hopes it offers are known by many to be illusory and although its promises are vain, communism derives its strength from those who, because of the inequitable distribution of incomes, have become the underprivileged of all lands. What other hope have those who are denied a substantial part of the fruits of their labor (in order that the perquisites of the privileged may be preserved) than that someone will somehow redistribute currently produced wealth in accordance with men's needs? The Marxian slogan, "From each according to his abilities; to each according to his needs," offers to the poor a hope comparable to the hope of a better world offered by many religions. Communism has the added advantage of promising to provide in this world now or in the immediate future what some religions offer only in the next world at some future time.

The strength of communism's appeal results from its promise to eliminate special privilege for the few and the inevitably corresponding inequality of opportunity and obvious inequity of reward for the many. Communism has grown in strength as special privilege has grown; the farther the nations of Western civilization have departed from equality of opportunity, one ingredient of freedom, the more they have drifted toward communism.

Facism often is discussed as though it were the opposite of communism, but such is not precisely the case. Hitler, Mussolini, and Stalin were different in many respects; but the principles of their economic ideologies were the principles of socialism; their initial appeal was to the underprivileged; and the final result, a new despotism, was the same in all three instances.

In view of the foregoing, we may summarize the present situation somewhat as follows: Western civilization as we know it today is the outcome of a great revolution that followed the acceptance of new ideas and that accompanied the progress toward individual freedom including equality of opportunity and economic justice[3] for all men. However, virtually complete freedom as herein described has not yet been reached except in relatively small areas of the world and even there only for brief periods.

Perhaps primarily because we of this civilization have stopped short of the goal, the results have in part been an inequitable distribution of currently produced wealth. In the minds of many, not even the material progress made possible by the great revolution can offset results that seem so evil. Either not realizing that the goal had never been reached or not understanding that the evils they deplored were attributable to *imperfect* freedom, many leaders in thought and action sought to turn back; thus the counterrevolution was born.

The counterrevolution is in progress throughout the world. It is clearly recognized as communism; but fascism, various Socialist governments, the New Deal, and the welfare state all have grown from the same roots.

Such is the situation at this point of the twentieth century. American foreign policy, if it is to be successful in the long run, must cope with the counterrevolution in Western civilization.

Lesson of the Immediate Past

Before proceeding to a discussion of American foreign policy, a brief review of recent developments will be helpful. A valuable lesson can be learned from mistakes of the recent past.

Germany and Russia were enemies in World War II, not because their ideologies differed, but because there was not room on the same continent for their ambitious rulers. We were allied with Russia, not because Russia was one of the democracies fighting for freedom, but because Russia happened to be fighting Germany and could be induced to fight Japan.

However, Americans are sometimes thought by their political leaders to be squeamish and unwilling to face the facts of life. Consequently, the wartime administration sought to "sell" the American people the notion that Stalin was a respectable companion in arms. They were not content to use him to the extent that he was useful, while keeping in mind that he was the leader of the counterrevolution threatening Western

[3]Economic justice refers to the third part of the definition of freedom previously given. Men who are free to plan and choose their goals and who enjoy equality of opportunities to seek their goals may be said to receive economic justice if they are permitted to retain the fruits of their labors.

civilization; they insisted on adopting Russia into the family of peace-loving nations. In their preoccupation with winning World War II, the Nation's leaders apparently closed their eyes to the important long-term developments that have been described here.

Our foreign policy during and immediately after World War II was a series of blunders precisely because we dealt with successive short-term situations as though there were no long-run fundamental conflicts of aims or as though we were blind to other than immediate pressing developments. Such was our major error, and the lesson should not be forgotten.

Prior to World War II, American foreign policy had to cope with two classes of potential enemies. The first included Germany and Japan as potential enemies for the same reason, ambition for power, that nations have so often been enemies throughout history. The other class of potential enemies may be roughly designated Communists or, to be more specific, the counterrevolutionary elements within Western civilization.

Fortunately, the problem of formulating an adequate foreign policy is simplified in some respects by the fact that, in coping with Russia as our only potential enemy of substantial strength in the first class (having a ruler whose ambitions for more territory and power make him a potential enemy), we shall be coping to some extent with the worldwide counterrevolutionary movement.

On the other hand, the situation is complicated by the fact that, in choosing a foreign policy intended to cope with Russia's ambitions for more territory and power, we may erroneously assume that the long-run problem of the counterrevolution is automatically solved merely because we associate the long-run problem also with Russia. Actually, the ruler of Russia is not the long-run problem; he is merely its temporary figure-head or symbol. Regardless of what happens to him or to Russia in the next several years, the long-run problem of the counterrevolution will remain.

What Can Be Done About Counterrevolution?

We now come to the question, "How can the foreign policy of one nation deal with counterrevolution within a civilization?" A nation faced with such a counterrevolution must choose one of three courses.

The first possible course is to join the counterrevolution. To a far greater extent than many people realize, the United States already has chosen this course. Many internal policies, especially (but not by any means solely) some of those adopted in the past three decades, conform to the principles advocated by the counterrevolutionists. In our foreign policies also we have not hesitated to give extensive financial aid to the political parties in control of various governments that are aiding and abetting the counterrevolution.

It should be apparent that the first possible course, which we have already chosen in part, will be self-defeating in the long run. If we encourage the counterrevolution in other nations and yield to its wiles at home, we shall end by joining wholeheartedly, while Western civilization declines and falls as others have done before.

The second possible course is to attempt to preserve the status quo, that is, neither to press on with the original revolution nor to join the counterrevolution. This apparently was an objective of the Truman policy. Although the Truman policy appeared to be somewhat inconsistent for several months, including as it did the extension of military aid to Greece and Turkey and the denial of military aid to Nationalist China and Korea, subsequent actions and announcements indicated that the policy had become firm. In essence it appeared to contemplate preservation of the status quo as of June 1950 indefinitely.

This second course, preserving the status quo, would seem to us impossible if we may legitimately deduce from history something other than that men *never* learn from history. And, aside from the lessons of history, we know that the conditions in which communism is rooted and from which it derives its strength have become increasingly favorable to communism; this trend seems destined to continue unless progress toward the goals of the great revolution is resumed. Preserving the status quo would become increasingly costly and increasingly difficult as the years pass. Such a policy is only a slower, not a less certain, road to destruction in the long run than the first possible course.

The third possible course is to oppose communism, but what effective means are there for opposing communism? An answer is not difficult to find if one remembers that communism is the ideology of the counterrevolution. Only if Western civilization presses on toward the goals of the great revolution will the circumstances that have fostered the counterrevolution be changed. Only as the source of its strength is reduced and finally eliminated will the counterrevolution be weakened and finally defeated in the long run.

Only the third course, to oppose communism by pressing on toward the goals of the great revolution within Western civilization, appears to be a practicable means of coping with the counterrevolution.

Fortunately, no other great nation is as well prepared as our own to undertake this task. In order to reorient our aim, we should study again the Declaration of Independence, the Constitution of the United States, the writings of Jefferson, and other documents, such as Lincoln's emancipation address, that have described the goals we once sought so eagerly. Then, we must ascertain why the goals have not been reached, why inequality of opportunity and an inequitable distribution of currently produced wealth became so marked even in the United States as well

as in the rest of Western civilization. Only then shall we be in a position to correct the fundamental errors in our procedure that have delayed progress toward the goals of the great revolution.

The United States has become a great nation, a tower of industrial strength in Western civilization, primarily because the goals of the great revolution were more nearly approached here than they were in Europe. In the greater material progress here in the United States, we have all around us tangible evidence that should more than justify the faith needed to press on. Surely we of all peoples of the world should know that freedom for the individual (not merely freedom from outside domination for a nation), equality of opportunity, and economic justice are among the important goals to be sought.

We have concluded that the only sound foreign policy for the United States in the long run is to resume our former place in the vanguard of the great revolution, to press on toward the goals of more nearly complete individual freedom, and to encourage other nations to follow. However, we shall be ill-prepared for such a position of leadership until we have reoriented the policies that we apply at home.

Too long have we yielded to the urgings of those who have joined the counterrevolution. Alger Hiss and others like him may not be traitors in the ordinary sense of that word, implying betrayal of their country in order to give advantage to a foreign enemy; perhaps they are merely miseducated men whose good intentions have led them to join the counterrevolution within Western civilization. We shall underestimate the potential danger if we fail to realize that such men are not misanthropic freaks but the legitimate products of some of the Nation's leading educational institutions.

Domestic Policy

Coping with the counterrevolution at home will not be easy. In order to regain the road toward the goals of the great revolution, we shall have to retrace some steps taken in recent years and turn aside from other goals toward which considerable progress has been made.

Specifically, corrective action will be needed along at least three general lines. First, the distortion of and interference with free market relationships must be reduced as rapidly as possible and ultimately ended; second, all special privileges must be eliminated; and, third, the activities of the Federal Government must be reduced to the role of national defense and prevention of license or abuse of freedom.

Restoration of free markets is essential if progress is to be made toward the goals of the great revolution. If men are to choose wisely among possible economic alternatives, they must be free to buy and sell at prices agreed upon among themselves without government intervention,

subsidies, or controls; they must be free to select, hold, and exchange the money or standard of value that they deem most suitable for the purpose (with men's customs and views as they are, the gold standard must be restored); and such abuses of the monetary system as inflation must be eliminated. For more than four decades Government intervention and "management" of the Nation's money-credit mechanism have resulted in progressively greater distortions and more extreme interference with free markets. The counterrevolutionists throughout the world have long regarded inflation as their most potent weapon; and events in Russia, Germany, France, and elsewhere have confirmed their judgment.

Holders of special privileges, especially those related to monopolies of natural resources (including land), under existing customs and laws acquire, at the expense of the producers, an expanding portion of the wealth currently produced. This situation results in increasing the number of underprivileged members at the base of society from whom communism derives its voting strength (but not, of course, its intellectual "front"), and it diverts from producers some of the means that could be used to increase production. Because the situation in this respect is more acute in various other countries, for example Italy, many observers see the problem there more clearly. Nevertheless, this problem is evident here in the United States and seems destined to become far more acute as the temporarily stimulating effects of prolonged inflation diminish.

Reduction of the role of the Federal Government to national defense and to the function of umpire for the purpose of preventing license or abuse of the principles of freedom is essential to the efficiency of the Government in performing its primary functions. United States Senators, who should have time for analysis and study of important policy matters such as those described here, spend their valuable time bickering over price-support levels for peanuts and innumerable other trivialities that have become the day-to-day business of an elephantine bureaucracy. A republic need not be as inefficient as a totalitarian form of government that attempts to control all economic activities; but, if we continue adding to the functions of our Federal Government as we have during recent decades, the fundamental efficiency of free men functioning in free markets will be replaced by the lumbering and creaking performance of a vast bureaucracy. We shall then be as inefficient as our totalitarian enemies.

Foreign Policy

For the purpose of coping with the immediate threat resulting from Russia's ambitions for more territory and power, our short-term foreign policy may well be based on the expedient, for the time being, rather than on principle. If war with Russia is imminent, we should not

scorn any allies, even one such as Spain. However, there is no need to repeat the silly process we went through when we used Russia as an ally in World War II; we need not fool ourselves that we are coping with the counterrevolution when we "make a deal" with men like Franco of Spain.

On the other hand, our intervention in Korea had no other excuse but as part of our long-run plan to cope with the counterrevolution. All of our military experts seem to be agreed that Korea would be a liability rather than an asset in the event of war with Russia in the near future. Obviously then, in Korea we should have insisted on pressing the great revolution, on progress toward the goals of individual freedom, equality of opportunity, and economic justice for all men. Was there any other goal in Korea worth the life of a single American soldier? (Surely our battle cry in Korea should not have been, "Restore to the landlords their vast feudal estates!")

If in doubt as to how progress toward those goals could be made in Korea, we might well study the situation in Denmark and New Zealand. The lessons we should learn would have the added advantage that they could also be applied here in the United States when we finally realize how badly we need to apply them.

Proposal for a National Policy Commission

Of course, the policies suggested here may not be generally accepted at first. The Nation's legislators who have been preoccupied with peanuts can hardly be expected to see world affairs in the perspective here described at first glance, and shallow or confused thinking about the problems of Western civilization in the twentieth century is by no means confined solely to the halls of Congress. Therefore, we raise the following question: Has not the time come for selection of a national commission on foreign and domestic policy? Such a commission, composed of the most competent men who can be drawn to its service could be expected to survey the entire problem of American foreign and domestic policy from a nonpartisan viewpoint. By means of extensive public hearings and discussion of various possibilities involved, public attention could be focused on these critical problems, and the public could become informed regarding these matters. Finally, before its work ended, such a commission could be expected to report findings and recommendations concerning foreign and domestic policy much as the Constitutional Convention did in 1787 or as the National Monetary Commission did on a less extensive scale fifty years ago.

Unless something like this is done, we greatly fear that the statue in New York Harbor of the goddess of liberty enlightening the world will no longer be an appropriate symbol of United States policy at home

or abroad. And, in that event, what shall it profit us if we gain widespread influence and for the time being stabilize the world but in so doing lose our own principles? We shall gain nothing but a little temporary security; but we shall lose all that we treasure highly if the United States declines and falls with the rest of Western civilization, a victim of the counterrevolution.

SUPPLEMENTARY NOTE

In the interests of avoiding confusion, we clarify below the differences in nature and purpose between the temporary commission proposed above and the permanent advisory council of behavioral scientists proposed in Chapter II.

The temporary commission on foreign and domestic policy would be appointed by the President under a formula for membership prescribed by Congress. (This is the procedure used in the past for temporary commissions of inquiry.) Thus it would be a temporary agency of the Federal Government with costs paid from Government funds.

If earlier precedents were followed, such a commission would include some members of Congress as well as experts and leaders in various fields including the military, academic, and business segments of the Nation.

Some of the questions that such a commission might consider would be these: Is the doctrine of preserving the status quo an appropriate foreign policy? Should the American people be taxed to support foreign governments whose objectives differ markedly from ours? Should atomic missiles be substituted for American troops in Western Europe? Precisely what areas of the world are essential to the national defense? Do we propose to fight to preserve the independence of every nation in the world, in effect to act as the world policeman?

These questions are intended to be representative rather than all-inclusive. The report and recommendations of such a commission could greatly aid in clarifying issues now too much obscured by political controversy and could aid the citizens in deciding policy issues of immediate pressing importance.

The proposed advisory council for scientific inquiry into the problems of men in society would be a quite different agency. It would be nongovernmental, nonpolitical, and nonrepresentative of any particular segments of the United States. All of its members would be scientists fully qualified in the application of modern scientific method in the behavioral sciences. The costs of this council would be met by the donations of individuals possibly supplemented by donations through colleges cooperating in administering such funds. The aim would be to make the council as nearly as possible independent of all ties to vested interests or particular segments of the Nation.

This council would *not* be responsible for recommending legislation nor would it function in any other way than as a source of advice for the citizens on the problems of men in society. Until recent decades, making such a council permanent might well have insured its ultimate uselessness. However, one of the most significant of recent developments in modern scientific method has been the realization by qualified scientists that useful answers rather than absolutely certain, incontrovertible, and everlastingly true answers are the fruits to be expected. By abandoning the notion that theirs is and will be the last word, modern scientists have provided for the self-correction that seems to be essential in view of man's still limited and still improving ability in conducting inquiries. In the absence of this self-correctional feature of modern scientific method, we should be reluctant to suggest that any council of inquiry be permanent.

IV.

FIRST STEPS TOWARD A SOLUTION

The United States is far along in a period of prolonged inflation similar to that in France since World War I.[1] In addition to the upward pressure on prices resulting from the great inflation, the excess purchasing media in circulation have made possible increases in some wages far beyond the point of balancing the increased output attributable to automation etc. Consequently, in spite of mass production on a larger scale here than anywhere else in the world, production costs are so high that American industries are at a disadvantage in foreign markets. Exports have decreased and imports have increased greatly. As a result, foreign holdings of claims on dollars have increased in spite of the fact that a large portion of the accumulating foreign claims has been used to demand gold from the Treasury.

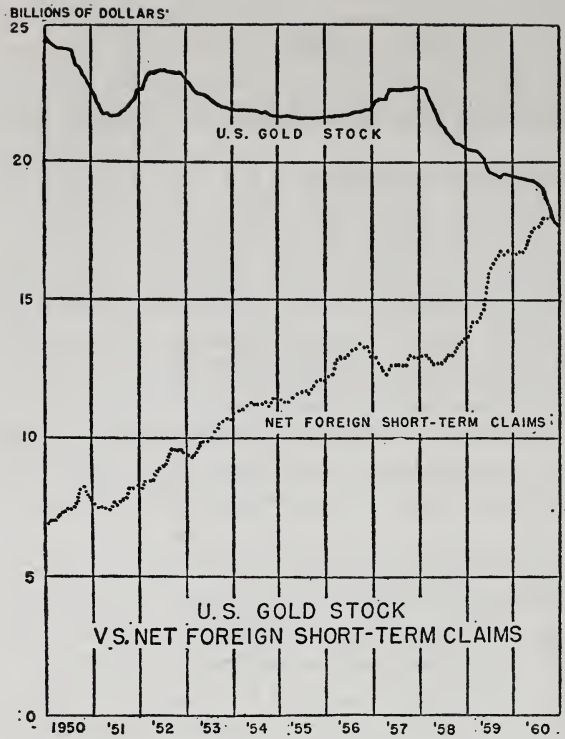
Now the potential foreign demand claims on U. S. gold, even after allowing for our demand claims on foreigners (which are very small), nearly equal our remaining supply of gold. In short, the United States already is nearly insolvent, insofar as its foreign creditors are concerned (see the charts on page 44). Thus has been incurred the risk of an international run on the dollar. Either as a result of ignorance and financial folly, or perhaps in part because of outright treason somewhere within our Government, the Nation has been placed in the situation that Harry Dexter White presumably sought to bring about when he arranged for Russia to have the plates for printing American occupation currency during World War II.

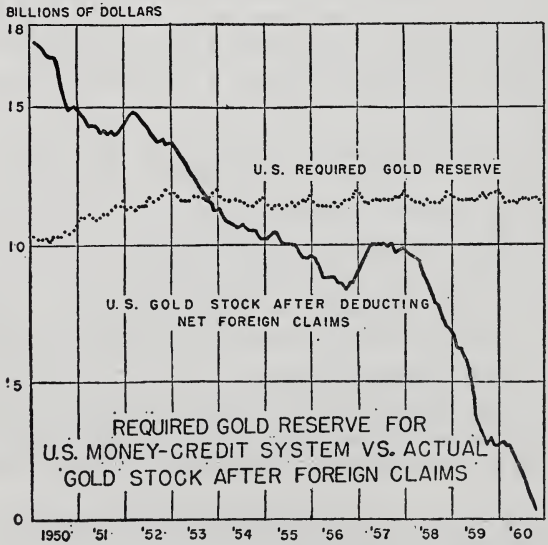
That the Nation's situation now is serious has been recognized by the Secretary of the Treasury and by some members of the Federal Reserve Board. In public statements these men have clearly indicated the dangers involved. Nevertheless, others within the Government have succeeded in continuing foreign aid, which will further increase foreign claims on U. S. gold. Evidently the highest echelon of Government has failed to understand the significance of the gold outflow and of the Treasury Secretary's great concern.

No one knows precisely when a financial panic or other major economic readjustments may be precipitated by events beyond the control of the United States Government. Nevertheless, we believe that months,

---

[1]Precisely how and to what extent the Nation's purchasing media (currency and checking accounts) have been inflated are shown in the chart on pages 90 and 91 and are explained in detail in Chapter X.


BILLIONS OF DOLLARS
25
20
15
10
5
0
U.S. GOLD STOCK
NET FOREIGN SHORT-TERM CLAIMS
U.S. GOLD STOCK
VS. NET FOREIGN SHORT-TERM CLAIMS
1950
'51
'52
'53
'54
'55
'56
'57
'58
'59
'60


BILLIONS OF DOLLARS
18
15
10
5
0
U.S. REQUIRED GOLD RESERVE
U.S. GOLD STOCK AFTER DEDUCTING
NET FOREIGN CLAIMS
REQUIRED GOLD RESERVE FOR
U.S. MONEY-CREDIT SYSTEM VS. ACTUAL
GOLD STOCK AFTER FOREIGN CLAIMS
1950
'51
'52
'53
'54
'55
'56
'57
'58
'59
'60

perhaps years, of crisis are ahead. Continued postponement of needed readjustments would only increase their ultimate severity.

During the crisis that lies ahead, the United States will be forced to make an important choice. The alternatives will be:

1. To continue inflating without regard to the loss of gold, thereby incurring the even greater risk of an internal flight from the dollar and accompanying economic collapse; or,

2. To deflate, either rapidly or gradually and thus restore balanced internal and external economic relationships.

Choosing the first alternative would reflect continued acceptance of the economic advice responsible for the Nation's present plight. Choosing the second alternative would reflect acceptance of economic advice from those who have repeatedly warned of the dangers incurred by continuing to inflate.

The academically and politically popular Keynesian economists have been the Nation's "medicine men" since 1934. Keynes' argument that "in the long run we are all dead," has been regarded by his enthusiastic followers as a sound reason for adopting their policies. But now we near the end of the short-run exhilaration provided by inflation, and the long run no longer is far away. Inflation involves a terrible price in the long run, and presentation of at least part of the bill seems not far distant.

The future of the United States may well depend on the answer to this question: Have the American people enough common sense to refuse to accept any more advice from those responsible for developments during recent decades and the present situation; will the Nation's citizens instead seek advice from the economists who have continually opposed the "perpetual motion" notions of the "creeping" and other inflationists? We don't pretend to know the answer to this question; only the citizens, or the better informed minority who hold the balance of political power, can provide the answer. All that we can do is outline a possible solution to the present problem, not an easy, painless remedy, because we know of none, but one that should provide a way out.

The first step should be to reassure the Nation's foreign creditors that another devaluation of the dollar will not be undertaken, in order to prevent a "run on the dollar." Mere words of reassurance would not be enough, however, because governments invariably issue such reassuring statements until a devaluation is accomplished. In this respect even the supposedly most responsible governments of the world have been completely lacking in what is ordinarily considered moral responsibility. There is no reason why foreign creditors should assume that the Government of the United States would be a paragon of virtue in this respect.

Actions rather than words will be required, and the following simultaneous actions are recommended:

a. The Treasury should continue to pay out gold on demand to foreign creditors, but they should be informed that licenses for gold withdrawals (the means by which the outflow can be controlled) will be limited to such amounts as will not jeopardize the United States by depleting its essential war and emergency reserves. (The exact rate of outflow, perhaps $100,000,000 per month or some such amount, should be no more than can be continued without danger during the interim period discussed below.)

b. Foreign creditors should also be informed that their demand claims on gold will be honored in the order received. Most of the short-term foreign claims now are invested in Treasury bills, savings accounts, or other interest-bearing obligations. Foreign creditors who desire to withdraw the gold they are entitled to would have to convert any such short-term investments to demand claims on dollars (i.e. to the form of currency or demand deposits) and present those claims to the Treasury for payment. Thus the foreign creditors would be penalized by loss of interest on all dollar claims presented for payment. This is the price they would pay for an earlier place in the waiting line, and presumably that would influence them in deciding what proportion of their claims they would present for immediate payment.

c. Announcement also should be made that the United States would return to the gold standard with full redeemability of its currency according to the promise on the face of it at the end of an interim period, perhaps 5 to 10 years in the future. Congressional action would be required, but there is a successful precedent for such action in the return to the gold standard after the Civil War. (In 1875 Congress voted to resume specie, i.e. gold, payments in 1879.)

This first step described in the paragraphs above, would tend to prevent an international "run on the dollar" and would provide an orderly means of coping with such a run if it occurred in spite of the precautions taken. Thus the present vulnerability of the Nation's gold reserves would be ended for the time being.

A second step would be necessary in progressing toward a long-run solution of the problem. This step should include the following:

a. Gradual deflating instead of further inflating. Monetization of Government debt and monetization of private long-term debt should end; and, over a period of years, part of accumulating savings should absorb the debt previously monetized. The commercial banks gradually should sell the investment-type assets (including mortgages and consumer loans) held in excess of the increasing capital funds and savings

or time deposits that justify the acquirement of such investment-type assets.

b. Accompanying the liquidation of excessive holdings of investments, the commercial banks should unhesitatingly enlarge their strictly commercial (short-term automatically self-liquidating) loans as may be necessary in order to provide purchasing media that can represent an increasing volume of things produced and en route to markets.

c. Of course, in the absence of more inflation and to some extent forced by gradual deflation, prices generally would decline. Thus, industries in the United States gradually could restore their competitive positions at home and abroad.

The success of the procedure outlined above will depend on various related developments including the following:

1. The Federal Government should spend much less than it collects in taxes and should steadily reduce its debt by a substantial amount each year. This would result in:

a. An immediate strengthening of confidence in securities issued by the Government with a resulting better market for such securities. Long-term financing at lower interest rates would be possible, and the savings in annual interest charges, which would be substantial, could be used to retire more debt. (The Nation's experience under somewhat similar circumstances after the Civil War demonstrated what may be accomplished.)

b. Government deficits to be financed by the commercial banks would be a thing of the past.

c. The better market for Government securities would facilitate demonetizing the debt previously monetized by the commercial banks, because institutional and other investors would more eagerly buy such securities from the banks.

2. In order to lessen Government spending as well as to terminate an experiment that has been disastrous and costly, the spending of billions to put more farm products in storage should end.

3. All proposed Government spending should be arranged in its relative priority and should be compared with the priorities for funds that might be better used in the hands of individuals and businesses for economic growth.

4. During gradual deflation with prices gradually declining, wage and salary earners should expect an increased standard of living to result from a decreasing cost of living rather than from rising wages. Some segments of the labor force probably would have to accept moderate reductions in wage rates if they wished to remain employed. If labor and management would agree on formulas for such wage

reductions where necessary, much strife advantageous to neither group nor the general public might be avoided.

Many readers may be surprised to learn that we confidently believe the Nation's economic growth would be increased under the conditions indicated above as it was during the period from 1875 to 1892 when a 35-percent decline in prices occurred at the same time as the highest and best sustained rate of industrial growth in our history. In any event, we should not expect a decline in prices during the next decade as great as the 35-percent decline from 1875 to 1892. Recent trends of gold production in the newer richer mines of South Africa suggest that the stimulation of gold mining attributable to decreasing costs would be followed by a great increase in gold output with a resulting tendency for the general decline in prices to lessen and finally cease as new gold entered the Nation's monetary system. Consequently, a decline in prices to pre-World War II levels seems highly improbable even if the deflation (cancellation of inflationary purchasing media) were rapid.

By the end of a decade at most, and perhaps earlier, sound money-credit conditions and a more healthy economy could be restored. This statement is not the expression of visionary hopes but is fully warranted by earlier experience of the United States. Moreover, the "miracle" of Germany's industrial recovery and subsequent growth since World War II, which is attributable largely to the restoration of more nearly free markets and a sound currency based on gold, should convince any qualified observer that the economic "medicine" the United States used in the decades following the Civil War is as effective today as it ever was, even in a nation where the industrial plant and equipment had been destroyed in substantial part by wartime bombing.

But perhaps the most important result that could follow in the longer run is a better opportunity for our Nation to correct long-existing maladjustments that have thwarted our efforts to progress toward the ultimate goals of a freely competitive (and therefore perfectly cooperative) society with equality of opportunity for all.

V.

STAND STILL, LITTLE LAMB, TO BE SHORN

The nearly half million readers of the Institute's publications are a large and probably representative sample of America's "forgotten men." They are "forgotten men" in the sense of William Graham Sumner's name for the ". . . quiet, virtuous, domestic citizen, who pays his debts and his taxes and is never heard of out of his little circle." These men are forgotten, that is, except when their votes are sought by those who would become the Nation's lawmakers and guardians of its Constitution.

From one point of view, however, the virtuous citizen who pays his taxes never is forgotten. His is the never-ending task of providing the funds for all public projects ranging from the necessary to the sometimes worse than useless. Moreover, largely on these citizens rests the burden not only of the taxes everyone knows about but also of that hidden tax attributable to a depreciating dollar, the inevitable result of inflation.

Apparently, few people realize the extent of this hidden tax. If the "forgotten men" understood the extent of this burden they are carrying, they would see how much they are relied upon by the beneficiaries of inflation and might, after recovering from the shock of counting their losses, develop a quiet pride in their burden-carrying capacity. Perhaps even a sheep develops pride in its ability to grow a good coat of wool, in spite of discovering that its fate is to be shorn.

The situation may be more calmly viewed by the victims of inflation if, instead of counting their losses, we count their contributions to the "success" of prolonged inflation. The fact that their contributions are made without their consent is an interesting aspect of the matter that perhaps makes "embezzlement" a more appropriate name for the process. However, different names do not alter the facts in the case.

The funds belonging to the Nation's "forgotten men" from which they contribute to the "success" of prolonged inflation are held largely in nine principal forms of investments. Each of these will be discussed in turn.

One of their largest single investments is in life insurance and annuities. The actual sum thus accumulated at any time is not the face amount of outstanding life insurance and annuity policies but the reserves held by the insurance companies for such policies. (Of course, from the beneficiaries' point of view, reductions in the buying power

of the dollar reduce the buying power of the face value of policies, also; but the policyholder himself directly loses, or contributes to the "success" of inflation, only the loss in buying power of the cash value of his policy.)

A second important investment made for individuals is the total of trust funds held by the Government for old-age pensions, employment and disability insurance, railroad retirement funds, and veterans' life insurance.

A third source from which contributions to the "success" of inflation are made is the total of savings or time deposits in the Nation's commercial and mutual savings banks. When the depositor is lucky, his loss of buying power in a year may be less than his interest earnings. In some years, however, the percentage depreciation of each dollar on deposit exceeds the interest earned during the year. In such years, the depositor contributes not only all of the interest he thinks he is earning but also some of his original capital. The stated amount of his deposit may increase as interest is added, but even the deposit thus enlarged will buy less than it would have at the beginning of the year.

A fourth principal investment likewise vulnerable to the thieving propensities of the inflationists is the total of accounts with savings-and-loan associations, with credit unions, and in postal savings. The dividend or interest return on these accounts in most instances has been greater than that on deposits in mutual savings banks, but even a larger return fails to counterbalance, in some years, the loss of buying power as the dollar depreciates.

A fifth principal investment is in the form of U.S. Government bonds. About two-thirds of the total held by individuals are the U.S. savings bonds so widely owned. For all government bonds, Dr. Franz Pick, the internationally-known expert on depreciating currencies, has coined the appropriate name "certificates of guaranteed confiscation." Once upon a time that name could not justly have been applied to the securities issued by the United States Government, but that was in the days when a gold clause guaranteeing repayment at maturity in dollars of the same gold weight and fineness was honored. Now this means of protecting the investor is illegal (except, apparently, for the U. S. Treasury when it chose to add a gold clause for some $500,000,000 of its securities sold to the International Monetary Fund in recent years).

A sixth investment made by the "forgotten men" is in bonds of States and municipalities.

A seventh investment is in the bonds of corporations.

An eighth investment is in loans secured by mortgages. (In order to avoid duplication, we of course include here only that portion of such mortgages held by individuals rather than the much larger total held by insurance companies, savings banks, and other financial institutions.)

HOW AMERICA'S "FORGOTTEN MEN" HAVE CONTRIBUTED TO THE "SUCCESS" OF INFLATION

(Data in Columns 2 to 12, inclusive, are as of January each year. Columns 13 and 14 show loss or depreciation during each year.)

1 YEAR	2 Life insur. policy reserves	3 Social Secur. reserves*	4 Savings depos. in all banks	5 Sav. & loan Credit unions, Postal sav.	6 U.S. Govt. issues held by indiv.	7 State & munic. bonds held by indiv.	8 Corporate bonds held by indiv.	9 Mortgages held by indiv.	10 Savings in cash & idle bank accounts	11 TOTAL † (billions of dollars)	12 Relative purchasing power of dollar ‡	13 % deprec. of dollar during year	14 LOSS of purchasing power §
1940	25.8	3.6	25.9	5.6	10.1	7.5	23.3	14.5	10.5	126.7	100.0	1.25	1.6
41	27.2	4.8	26.5	5.8	10.6	7.3	22.9	14.8	13.3	133.3	98.8	10.02	13.4
42	28.9	6.5	26.5	6.3	13.6	7.2	22.0	14.8	14.9	140.7	88.9	7.25	10.2
43	30.8	9.2	27.1	6.7	23.7	7.0	22.0	15.0	21.5	162.9	82.5	2.89	4.7
44	33.0	12.9	31.1	7.7	37.6	6.9	21.4	14.5	32.7	197.7	80.1	2.16	4.3
45	35.6	17.7	37.6	9.1	53.3	6.8	20.2	13.8	43.1	237.0	78.3	2.13	5.0
46	38.7	21.1	45.6	10.8	64.1	6.5	18.6	14.0	53.2	272.5	76.7	15.40	41.9
47	41.7	24.0	50.8	12.4	64.2	6.3	17.4	17.8	48.7	283.2	64.9	9.29	26.3
48	44.9	26.7	53.1	13.8	65.7	6.7	16.7	18.1	45.2	290.9	58.6	1.32	3.8
49	48.2	28.6	54.3	15.0	65.5	7.9	17.3	18.5	41.8	297.0	58.0	2.05+	6.1+
1950	51.5	28.0	55.6	16.5	66.3	8.8	17.4	19.2	43.1	306.3	59.2	7.34	22.5
51	54.9	30.8	56.5	17.9	66.3	10.0	19.3	20.0	37.6	313.3	54.9	4.02	12.6
52	58.5	33.5	59.0	20.0	64.6	11.3	21.3	20.8	39.5	328.5	52.7	0.68	2.2
53	62.6	36.1	63.6	23.1	65.1	12.5	23.5	21.5	38.8	346.8	52.3	1.14	4.0
54	66.7	37.8	68.4	26.9	64.9	13.8	25.5	23.3	39.5	366.7	51.7	0.81+	3.0+
55	70.9	38.5	73.5	31.6	63.6	16.2	26.5	25.2	37.4	383.4	52.1	0.23	0.9
56	75.4	40.5	76.8	36.6	65.3	18.6	28.8	27.6	30.0	399.6	52.0	3.09	12.4
57	79.7	41.7	80.9	41.8	66.1	20.7	32.3	30.0	25.0	418.2	50.4	3.31	13.8
58	84.1	41.0	88.1	46.7	65.7	22.6	35.7	32.4	21.3	437.6	48.7	1.22	5.4
59	88.6	39.3	97.5	53.0	63.5	24.7	38.3	34.8	19.9	459.6	48.1	1.61	7.4
1960											47.4p		
										Total loss in billions of dollars ——			183.3

* Funds held in trust for individuals by U.S. Government (Social Security, disability and life insurance, and retirement funds).
† Fixed-dollar-value assets held by individuals (total of Columns 2-10, inclusive).
‡ Taking the January 1940 dollar as equal to 100.
§ These are the "contributions" (in billions of dollars) during each year.
p Preliminary.

A ninth form of investment includes the currency hoarded by many individuals, who prefer thus to accumulate their savings, and the inactive or idle checking accounts in which individuals sometimes accumulate funds for future purchases.

In the table on page 51 we show for the beginning of each year the amount in each type of investment. The total of all types combined is shown in column 11. In column 12 we show the purchasing power of the dollar, taking its January 1940 buying power as 100 cents. In column 13 we show the precentage reduction of the buying power of the dollar during each year. Then, in the last column, we show the dollar loss of buying power, the contribution to the "success" of inflation for each year.

That such contributions to the "success" of inflation total nearly $200,000,000,000 since 1939 may surprise most readers. If the Nation's "forgotten men" comprise about half the population, this forced contribution approximates $10,000 per family involved. In relation to the Federal income tax on individuals, the losses on savings alone that are attributable to embezzlement via inflation would equal such taxes for 4 or 5 years at the current rate.

If this huge supplementary tax, this forced contribution, made the process of inflation successful in stimulating sound and sustainable economic growth at a faster rate than would otherwise be possible, the results might be worth the price. But there is no instance in the known history of the world when such was the outcome. On the contrary, every prolonged inflation has fostered maladjustments such as those obvious in the United States today. Not sound, sustainable economic growth but unbalanced, maladjusted "boom" prosperity, unsound and always temporary, has been the result of prolonged inflation at all times and without exception.

Some readers may question whether the results are as bad as the foregoing implies. After all, the prosperity of recent years has been real enough; most people actually do have more things to enjoy than they ever had before; the new cars and new homes are real even if they have been acquired by borrowing at a rate never before equaled. Some people may ask, if that contribution of $200,000,000,000 fostered such widespread prosperity, wasn't it worthwhile; the loss of savers' buying power is bad, but it might have been worse, mightn't it?

As a matter of fact the situation is worse, much worse than is indicated by the nearly $200,000,000,000. That is only part of the loss and perhaps the smaller part at that. Not only did the "forgotten men" lose that amount from their accumulated savings, they and others lost still more from their current incomes. All whose incomes increased less rapidly than did the cost of living lost still more, an

amount difficult to ascertain but assuredly large. Those whose incomes were relatively fixed, those dependent on pensions, annuities, income from bonds, and on salaries or wages that were not increased as rapidly as the cost of living rose, all those many millions of individuals also were forced to contribute to the "success" of prolonged inflation.

But to revert to the tangible evidence of widespread prosperity, what does it reveal? Simply that some have benefited at the expense of others and have obtained in the form of goods for immediate consumption wealth that, in order to sustain sound economic growth, should have been invested in such things as roads, schools, colleges, and the more efficient factories that would help the United States maintain its position in a competitive world. To an extent difficult to measure, the citizens' savings that should provide the Nation's economic growth and the protection of dependents as well as retirement pensions have been drawn upon for current consumption.

Everyone who saves knows that he could have another car in his garage, more expensive vacations, more steaks, and a higher standard of living generally if he would spend instead of save, draw on his past savings, and incur debt to buy more things today. Something much like this has been done during the past two decades. The principal difference is in the fact that instead of the savers withdrawing their accumulated funds to spend currently, the withdrawing has been done by the beneficiaries of inflation through the subtle embezzlement that is an aspect of inflation. Specifically, while the Nation's savers thought they were adding about $333,000,000,000 to their savings from 1940 to 1959, the beneficiaries of inflation were embezzling $183,300,000,000 from the buying power of the funds saved.

The Institute has recommended means by which some of the Nation's "forgotten men" might protect part of their funds against the depreciation of the dollar. Gold held abroad and stocks of the better gold mining companies, if purchased at reasonable prices, can provide some protection against either another devaluation (reduction in the gold weight) of the dollar or a severe recession, the aftermath of prolonged inflation follies. However, such uses of funds involve sacrifices and risks. Investments in gold bring no dividend or interest return and involve small annual charges for safekeeping. Investments in stocks of gold mining companies abroad (few are available now within the United States) involve risks of political uncertainties as well as other risks largely eliminated by investing at home. For the individual who can afford loss of income or the risk of foreign investments, gold or gold stocks, or both, offer partial protection; but such savers are only a small portion of the Nation's "forgotten men." How can the more numerous others find protection?

A little more than a quarter century ago, when the Institute first began calling attention to the probability of great and prolonged inflation, an answer was easy to find. We recommended and continued to recommend for many years that the Nation's "forgotten men" buy common stocks as a principal means of obtaining protection against inflation. Even after World War II, when many were warning of a postwar depression ahead, we urged retention of common stocks because we believed that the effects of the wartime and postwar inflation would continue for years. But by the end of 1959 common stocks generally had risen far above former peak levels. We no longer considered it safe to assume that buying stocks surely would provide protection against inflation and recommended that any prudent man reduce his holdings of common stocks to about one-third of total funds.

What can the ordinary "forgotten man" do? We refer to the individual who has life insurance protection for his family, a few thousand dollars saved for the education of his children, and perhaps several more thousand dollars saved for his retirement years. Unfortunately, we do not believe that there is any wholly satisfying answer for such individuals. For the small portion of their funds that might still be invested in common stocks, we have no doubt that shares of the better closed-end investment companies now available in the market at a discount below net asset value are the best investments. But for most of their funds, especially those assets intended to protect their dependents, we know of no fully satisfactory solution to their problem.

Indeed, if they will but reflect on the situation, the Nation's "forgotten men" will realize that they cannot obtain protection against inflation. The beneficiaries of inflation depend on the victims to provide the real wealth that inflation embezzles. The "forgotten men" are the sheep to be shorn.

You, the reader, may object that you are not a sheep but a man. In one sense of the word, what you say is true, but as long as you act like a sheep by accumulating more "wool" (assets in fixed dollar value) that can easily be shorn and by failing to protest against the shearing process, in all probability you will be shorn like a lamb whether you like it or not.

Many people ask us, "But what can I do, I am only one citizen, I am all alone." The Nation's "forgotten men" are not alone; they number many millions. If that were not so, they would not have so much that can be transferred to the beneficiaries of inflation. On the other hand, the farmers today *are* a small minority, and only a few of that small minority benefit on a large scale from the farm programs; but the politicians heed them because they act, if not more like men, at least more like hogs than like sheep. They make known their desires, and the politicians heed them.

(We do not imply that the few farmers who are collecting many thousands of dollars each from the public trough are the only "hogs" so occupied. From an economist's point of view, all who clamor for special privileges at public expense belong in the same classification.)

The fact is that the power of the Nation's "forgotten men" is vastly more than they seem to realize, enough to change the course of history whenever they choose to act like men instead of like sheep. In West Germany the "forgotten men" after two thorough shearings via inflation (in 1923 and again two decades later) finally insisted on an end to inflation; and they now have both a rapidly growing economy and a currency for which they can obtain gold on demand.

Does this imply that in West Germany the politicians are better informed than those in the United States on money-credit matters or are more diligent in voluntarily protecting the "forgotten men's" interests? Not at all; statesmen are always on the side of the "forgotten men" in any event, but politicians are alike the world over. Politicians don't have deep-seated convictions; they are keenly alert to the desires of any group that may hold the balance of political power in an election district. When such a group, especially if it is as numerous as are the Nation's "forgotten men," manifests definite desires, the politicians will be eager to vote as the "forgotten men" wish.

Some readers may suggest that many politicians already have evidenced their intention to stop inflation. This raises the question, what is satisfactory evidence of such intentions? No one should assume that words, however sincere they may seem to be, are sufficient evidence. Vigorous advocacy of and actual voting for restoring the gold standard for the Nation's currency at the earliest practicable date (perhaps setting a date 5 to 10 years in the future because of the many inflationary maladjustments to be corrected) would constitute, in our opinion, the only worthwhile evidence of an intent to stop inflation. As we interpret them, mere oratorical condemnations of inflation by politicians and assurances that the dollar will not again be devalued (like Sir Stafford Cripps' several denials that the pound would be devalued, the last on the day before that action), in short, all verbal shadowboxing with inflation can be translated thus, "Stand still, little lamb, to be shorn."

VI.

CAN FARMERS BE SAVED FROM THEIR POLITICIAN FRIENDS?

Well might the American farmer exclaim, in the words of the old English proverb, "God save me from my friends; I can take care of my enemies." The farmer's enemies — bugs, weeds, and weather — have but a limited power to harm. Even the worst drought has ended in a few years; weeds can be fought with modern chemicals; and grasshopper plagues rarely destroy two crops in succession. But the farmer's politician "friends" have created a farm problem beyond the ability of any one farmer or all of them put together to solve.

Of course, a small minority of the farmers do not want the farm problem to be solved as long as the U. S. Treasury will continue to pour cash into their pockets. Senator John Williams of Delaware recently inserted in the Congressional Record a list of 297 recipients of price-support loans ranging up to $1,442,595 in one instance, with many in the quarter million dollar range and higher. Three of these "farmers," the Senator reported, received more than the Government loaned to all farmers in the States of Delaware, New Jersey, and Pennsylvania combined.

Professor William H. Peterson of New York University has completed a remarkable study of the great and tragic attempt to solve the farm problem by government intervention. In a book that every citizen who wishes to be well-informed should read, the story is presented in its full historical perspective.[1] *And in an article for* Human Events, *Professor Peterson summarized his findings.*[2] *With permission of both the publishers concerned we reproduce the following extracts from these sources.*

Excerpts From Human Events

For more than a generation, ever increasing surpluses — a telltale sign that something is wrong — have dogged the agricultural experts in Washington. The year 1958, a bumper-crop year, provided the biggest farm surpluses of all time. Each time the planners hopefully believed that victory was at last theirs, with surpluses declining or even "stabilized," new obstacles appeared.

---

[1]William H. Peterson, *The Great Farm Problem,* published by Henry Regnery Company, Chicago, (Copyright 1959), price $5.00.

[2]*Human Events,* Vol. XVII, No. 3, January 21, 1960; 404 First Street, SE., Washington 3, D.C., price 20 cents.

Mountainous obstacles. Adequate storage facilities were not, for long periods, to be had. In the early days of the Eisenhower Administration, caves, abandoned factories, hangars, circus tents, oil tanks, mothballed World War II merchant ships, walled-up rural streets, and shutdown movie houses supplemented existing grain-terminal and elevator space. The ships-into-bins use continues to the present moment.***

In May, 1959, the Government owned or had a lien on more than $3 billion worth of wheat and more than $2 billion worth of corn. As of February 28, 1959, Department of Agriculture statisticians estimated the Government-owned Commodity Credit Corporation's "investment" in the Nation's wheat at better than a billion bushels***. The Commodity Credit Corporation's "investment" in corn was also well over a billion bushels***.

All in all, the Government's total "investment" in farm commodities runs over $9 billion. By June 30, 1963, under present laws, the USDA expects the Government's stake in farm surpluses to climb to about $12 billion.***

* * * * * * *

Farm surpluses are three-and-one-half times as large as they were at the beginning of 1953. Carrying charges — storage, transportation and interest — cost the Government more than $1 billion annually.

* * * * * * *

Thus intervention is the farm problem. The problem is strictly political. Were there no intervention, there would be no farm problem. Of course there would be the perennial agricultural problems of weather, insects, erosions, competition, shifting consumer tastes, the relative efficiency and inefficiency of individual farmers, fast-moving farm technology, and so on.***

Intervention, by way of definition, is governmental interference with the market forces of supply and demand. It is carried out directly or indirectly by the Government. Intervention occurs, for example, when public agencies enter the market place and set minimum or maximum prices or tax one group of competitors (e.g., foreign) and not another. Intervention occurs, too, when Government tightly "regulates" otherwise competitive industries through political appointees or grants privileges to such groups as industrial cartels or labor unions in order to protect them from competition — i.e., grants them monopoly power.

The tragedy of all interevention — the farm problem is a case in point — is that the longer it continues, the more difficult it becomes to extricate producers, consumers and the Nation from the growing morass of controls and politics. Intervention breeds intervention. Politicians may clothe farm-intervention in semantic niceties, such as "parity

prices," "Soil Bank," "Brannan Plan," "Food Stamp Plan," "ever normal granary," "soil conservation," or simply, "farm policy," but the basic disruption of market forces — intervention — continues.

Farm intervention dates back, mainly, to Hoover's Federal Farm Board of 1929. For 30 years — 1929 to 1959 — intervention has, rather than solve the farm problem, exacerbated it.

* * * * * * *

The United States Government, through thousands of its agents in county seats, buys much of the Nation's grain. It lets farmers know how many acres they may plant, with inspectors checking in the field to make sure there is no overplanting. It insures crops. It stores crops. It irrigates crops. It sells crops. It exports crops. It gives away crops — for example, through foreign aid and the school-lunch program. It plans and finances soil conservation. While fretting over surpluses, it researches for greater corn yields, and it annually adds vast new acreage of farmland through its land-reclamation program. It lends money, at subsidized rates, to farmers for equipment, electrification, livestock, planting, seed, fertilizer, and harvesting. It restricts domestic competition. It exempts co-operatives from corporate income taxes and the anti-trust law. On certain commodities — fluid milk, for example — it directly sets minimum prices. Through price supports it indirectly sets prices on all other so-called "basic" crops.

The farmer is no longer a free agent. Neither is the consumer. The consumer is forced to support the waste of intervention through higher taxes and artificially higher prices for farm products.***

Excerpts From Professor Peterson's Book
The Great Farm Problem

Farm intervention, by way of example, begins in a mild enough way. We shall raise farm income, say the farm interventionists, merely by providing cheap credit. This fails to prop farm income, for the marginal and submarginal producers thereby get a subsidy sufficient to hold them on the land and thereby worsen the surplus problem. Next, the farm interventionists try transportation-rate concessions, tariff protection, various tax exemptions, and stimulation of co-operatives. All fail. Price-fixing schemes and, inevitably, massive surplus-control and disposal problems result. Intervention piles on intervention, with, finally, the basic freedom and vitality of farming thoroughly smothered.

For this reason, the author recommends the elimination of market intervention, the abandonment, to use the words of the Supreme Court, "with all deliberate speed" — say over a four year period — of all price supports, commodity loans, conservation payments, acreage allocations, marketing controls, price-fixing, cheap credit, tax concessions, crop in-

surance, and all other government dictates and subsidies, open and hidden, to farmers. The USDA should be an advisory agency, not a price or income arbitrator.

That this recommendation is not so radical is evidenced by a poll conducted by *The Farm Journal*, one of the largest national farm magazines, and referred to by Secretary Benson in a speech in Dallas in 1959. Earlier in the year, the Journal invited farmers to tell Congress what to do about price support programs. In replying to that poll, 55 per cent voted for "no supports, no controls, no floors, free market prices; get the government clear out."*** (pp. 198-199)

* * * * * * *

Price supports as an integral of farm intervention are essentially a form of price-fixing. The futility of price-fixing was signaled long before the 30-year fiasco of "farm policy" beginning with the Federal Farm Board of 1929, as demonstrated by Mary G. Lacy. In March of 1922, Miss Lacy, librarian for the U. S. Department of Agriculture's Bureau of Agricultural Economics, delivered a paper entitled "Food Control during Forty-Six Centuries" to the Agricultural History Society.***

In her paper, Miss Lacy retold the well-known Biblical story of Joseph, which shows how the progressive control of the food supply by the Egyptian government reduced the Egyptian people to slavery three millennia before Christ. Miss Lacy's paper is replete with examples of the dangers of governmental interference with the production and sale of food. From 404-337 B.C., for example, Athens commandeered the grain trade and set price maximums but, despite extreme penalties, was unable to enforce them.*** (p. 205-206)

* * * * * * *

The French Revolution was plagued by inflation arising directly out of enormous issues of paper currency. Rather than stop the inflation at its source, Robespierre and his advisers preferred to treat symptoms — prices, especially the prices of food. Proclaimed Robespierre: "The food necessary to man is as sacred as life itself." And, "The fruits of the earth like the atmosphere belong to all men."

For reasons previously discussed, famine quickly fanned out along the streets of Paris. Price-fixing and its inevitable concomitant, the black market, became two of the many lethal aspects of the Reign of Terror.***

Sometimes the lesson catches hold, if only temporarily. In 1770, the government of Lower Bengal had acted to restrain what it termed the monopoly of rice when that crop failed. Speculation in rice was forbidden and the price of rice was strictly controlled. The result was unforeseen; one-third of the population perished. Higher prices,

which could have prevented much death and suffering, were not forthcoming. Higher prices would have rationed consumption and would have induced other parts of India and Asia to ship in grain. But the low maximum price set by the Bengalese government couldn't even cover the cost of transportation.

Very different was the action of the authorities when in 1866 another crop failure was experienced in the Bengal region. Far from trying to check speculation, the authorities did everything in their power to stimulate it. In the earlier famine, no one entered the grain trade in view of the price law. In 1866, many entered the trade, which the government expedited by publishing the free market grain rates in every district to render trade safe and easy. It was therefore common knowledge where grain was cheapest to buy and dearest to sell. The upshot was that the price of grain advanced by a few farthings, much less than the controlled prices at the end of the earlier famine, and virtually nobody died of starvation. (pp. 207-209)

The summary on the closing pages of The Great Farm Problem *contains a list of numbered conclusions. From this recapitulation of Professor Peterson's argument, we have chosen the following statements with which to end our quotations from his well-organized and illuminating book.*

Price, acreage, and marketing controls have proved inept and ineffectual, partly because of technology, partly because of politics, partly because of farmer circumvention, and mainly because of their inherent contradictions.

The Soil Bank, measured by its stated objectives, has failed. In 1958, for example, on the smallest acreage in 40 years, U. S. farmers harvested the largest crop output on record.

Parity has been a misconception from the outset.

"Farm policy" has destroyed many of the farmer's markets by overpricing agricultural commodities and by subsidizing, in effect, foreign and synthetic competition.

The real farm surplus is surplus farmers. Price supports perpetuate this surplus as would various alternative subsidies such as the Brannan Plan and other direct payment schemes.

The small marginal farmer, long the object of government paternalism, may someday be as passé as the village blacksmith.

"Farm Policy," measured by its stated objectives, is a thirty year failure and a hopeless patchwork of laws which frequently operate at cross-purposes.*** In the 1957 crop year while the Government was loaning $3,447,902.81 to support the crops being produced by ten

companies, another Government agency was under a different program paying these same companies $557,495.35 for not producing crops on another 10,243.6 acres which they controlled.

Many farmers grow for Government storage and not for market consumption, and hence become less concerned with the quality of their product. To wit: There has been a sharp increase of "yellow-belly" wheat (i.e. inferior quality) moving into Government inventory.

The cure for low prices is low prices; "the cure for 10-cent cotton is 10-cent cotton." The healthiest part of the American farm economy (more than half) is the part which does not get the "benefit" of mandatory price supports. The free market is the only way out of the farm problem.

Intervention is rarely, if ever, self-contained.

Farm intervention in America is but a phase of general intervention or statism. Statism is incompatible with human freedom, and since it hobbles economic proficiency, it is a poor answer to the Soviet economic challenge. (pp. 211-212)

* * * * * * *

The tragedy of modern farm intervention is twofold. One tragedy stems from man's efforts, in a sense heroic, to repeal Nature's laws, to substitute bureaucratic rule for the market place, to set prices below the market price and decree, vainly, that there shall be no shortage, and to set prices above the market price and assert, again vainly, that there shall be no surpluses.*** Politics enters (e.g. the farm bloc). Pressure groups pull this way and that. One intervention fails, and a new one is taken on. The jerry-built edifice wobbles anew. So still more intervention.

A generation of "farm policy" adds up to hopeless tinkering, fantastic losses, planned chaos, a lost war against Nature's laws. The battles have been man's laws: the Fordney-McCumber Tariff, the McNary-Haugen bills, the Farm Marketing Board, the Smoot-Hawley Tariff, the A.A.A., soil conservation, the ever normal granary, the Food-Stamp Plan, 90 percent of parity, the Brannan Plan, flexible parity, the Soil Bank, overseas surplus disposal. These man-made laws have snares. Tens of thousands of American farmers run afoul of the farm laws every year.***

The irony is that the farmer to be saved wasn't; since the New Deal, one of every three farmers has quit. The exodus from farming, in a sense a triumph of efficiency over intervention, continues to the present day.

The second phase of the tragedy of modern farm intervention is that it is but a chapter in a much longer unfinished story; it is a part of a philosophy, a way of life, a return to mercantilism, a recall

to the planned society of Imperial Rome. How will the story end? (pp. 216-218)

Suggested Program

So much for Professor Peterson's well-expressed views. We think it not difficult to predict how the story will end. But first we offer our suggested modification of Dr. Peterson's program. Instead of a gradual transition, we believe much is to be gained from a more rapid transition as follows:

a. Remove all price supports, all guarantees, and all acreage and marketing controls at the end of the present contracts. This is his first step.

b. Instead of selling all Government holdings of surplus crops back to the farmers, however, use the crops to pay farmers, in kind, for crops not planted in the next or succeeding years. Let those farmers who accept stored wheat, for example, in lieu of growing more, spend a season in other work on their buildings, their land, or if they choose in nearby industries; but, in any event, let the surpluses replace crops that otherwise might be grown thereby quickly restoring normal supply-and-demand conditions in free markets.

c. Reduce taxes by the amount of the savings in agricultural benefits with special attention to lessening the retarding effects of present taxes on business expansion (thereby providing more opportunities for surplus farmers in industry) and let individual citizens benefit by the substantially lower food prices that will help them to balance their budgets.

In considering this problem, many people seem not to realize that the farm operators number fewer than 5,000,000 in the Nation's population of 180,000,000. More than half of the farm operators do not share in Uncle Sam's beneficence but lose because they must pay unnecessarily high prices for cattle and poultry feed, for example, and because, like the rest of us, they buy most of the food for their families. A small minority of the minority who do benefit "skim the cream" from the farm program as Senator Williams has said.

Reverting now to how the story will end if common sense does not supersede Government intervention, the outcome in that event is certain. Encumbered by increasing controls and other hindrances to free markets, the economic growth of the United States surely would be retarded further. Within a few decades at most, our Nation might become a second-rate power, doomed to destruction by its own folly.

VII.

PUTTING FRIENDS IN SOCIALIST STRAITJACKETS

What has been the general tendency of American foreign aid? Have the economic results been those desired by the American people? Can our friends survive American aid or will they be forced into Socialist straitjackets for ultimate incarceration in the Communist madhouse?

These are not rhetorical questions, nor are they trick questions to awaken reader interest. They reflect serious doubts that arise from some of the facts of foreign aid. We shall explain the reasons for these doubts and, to the extent that we can, shall suggest answers to the questions.

Great Britain

Consider first the case of aid to Great Britain. In July 1945 the British Labor Party won a great victory at the polls, and Mr. Attlee formed a government that was to remain in power until October 25, 1951. Soon after assuming office the Labor Government embarked on its grandiose plan to establish socialism in Great Britain by nationalizing major industries.

An official estimate placed wartime property damage at $5,800,000,000 based on 1946 replacements costs. The United States promptly provided $5,169,000,000 in loans and grants, nearly offsetting the entire amount of the wartime damage. In the final two years of the Labor Government's term in office, the United States provided an additional $872,000,000 making the total $6,041,000,000. (These amounts do not include military aid.) In other words, to the Labor Government determined to establish socialism in Great Britain, the United States provided aid at an average of $1,000,000,000 per year, a total in the 6 years of about $600 for every family in Great Britain.

In spite of this aid from the United States at a rate never before equaled in the history of the world, the Labor Government with its socialistic endeavors was unable to foster economic prosperity in Britain. Wartime rationing was continued throughout the Labor regime. Even by 1951 industrial production was only 20 percent more than the prewar rate, compared with gains of 50 percent for Italy and the Netherlands where wartime destruction had been roughly comparable. Economic growth in Britain was less than that of almost any other nation in Europe.

In 1950 the Labor Government reached the end of its term, and general elections were held. By a narrow margin, Labor remained in power. Although socialism as a national policy was a failure, American aid had forestalled the economic difficulties that otherwise would have resulted, had enabled the Labor Government to complete a full 5-year term, and thus had postponed the complete discrediting of Socialist experiments that must have resulted had our aid been substantially less. Only a year and a half later the situation had become so bad that the Labor Government no longer could retain control, and general elections were called. The Conservatives then won by a narrow margin, a victory that assuredly would have occurred much earlier but for the American aid that bolstered the Labor Government.

For the next 5 years under a Conservative Government, American aid was provided at the average rate of $170,000,000 annually, about one-sixth of the average rate during the Labor regime. The striking contrast suggests: either (1) the policies of the Conservative Government (which included discontinuing rationing and returning the steel and road transport industries to private ownership) were so successful that aid was no longer needed; or (2) American authorities had been eager to help force Britain into a Socialist straitjacket but were reluctant to help a free-enterprise government succeed.

If the first answer is correct, i.e. that non-Socialist policies were successful and greatly lessened the need for aid, a question arises as to why the American authorities failed to assume so in the first place. Why the foolish faith in and eagerness to help socialism rather than confidence in a free-enterprise economy? If the second answer is correct, why is the United States employing policymakers so dedicated to socialism that they are doing what they can to force Socialist straitjackets on our friends and allies? Are such public servants adequately serving the interests of the United States?

West Germany

The situation in West Germany differed greatly from that in Great Britain. The occupying powers in the Western Zone (France, Great Britain, and the United States) finally gave up trying to function with Russia's cooperation after a series of Russian vetoes of proposed policies.

In the spring of 1948, France, Britain, and the United States invited the Netherlands, Belgium, and Luxembourg to develop new economic and political policies for Western Germany. These powers decided to establish a republic, to reform the money-credit system, and to end inflation by introducing a new mark. The West German Republic began operations on May 23, 1949.

From the end of World War II until the West German Republic

was born four years later, the occupying powers controlled political and economic policies in West Germany. The dismantling of industry proceeded along with rapidly increasing inflation of the currency in a network of price controls and rationing, the combined effects of which would have strangled even the healthiest economy. Thus was economic sabotage added to the disruptive effects of wartime bombing.

In Germany more than 40 percent of the housing was either badly damaged or completely destroyed. The Ruhr, the industrial workshop of Germany, was a vast heap of rubble. Official estimates placed the damage at more than $50,000,000,000 in 1946 prices and probably nearer $75,000,000,000. In other words, the damage was at least 10 times that in Great Britain. (The population and industrial development of West Germany and Great Britain are approximately equal.)

An official publication of the United Nations (*Economic Survey of Europe Since the War,* Geneva, 1953) reported on the situation in West Germany as follows:

"In that country, the practice of 'suppressing' inflation was carried ad absurdum to the point of strangling economic activity. ***Money ceased to a great extent to function either as a circulating medium or as a measure of economic calculations.*** The result was twofold; an extremely slow recovery of industrial production and a wide disparity between easy food conditions in the countryside and starvation in the towns." (p. 73)

Gustav Stolper in his book *German Realities* said:

"The root is the gruesome fact that German economic life has been kept in a straitjacket which stifles the best intentions of the occupying administration and the most intelligent German initiative.*** Here, ***we can study what happens to a bureaucratically directed economy once the regulative forces of money and the market are abandoned. (p. 75)

"American public opinion is hardly aware to what extent America's German policy has been shaped by Marxist ideologies, slogans and propaganda." (p. 177)

Naturally, the burden of preventing widespread starvation fell on the occupying powers, and that of course meant on the United States. From 1946 through 1949 this expense to the United States exceeded $3,000,000,000. Obviously that sum could hardly have begun repairing the war damage because much of it was used simply to prevent starvation and alleviate economic distress directly attributable to unwise socialistic policies.

When the authorities of the West German Republic assumed their duties in the fall of 1949, the drastic deflation that began in late 1948 was bringing order out of chaos. By applying the principles of a free-market economy, the West German Government demonstrated its align-

ment with the basic economic principles of the United States Constitution and fostered economic recovery on a scale seen nowhere else in Socialist-ridden Europe. Again the United Nations report is enlightening:

"The monetary reform in June 1948 completely changed the picture. Owners of speculative stocks of goods were forced to sell, and the increased supply of raw materials made a considerable rise in industrial production possible. Farmers became more willing to market their products, and the improved supply of both food and industrial goods increased the incentive to work.***

"The effects on industrial production were dramatic. If the statistics are taken at their face value, it rose by nearly 50 percent during the second half of the year. Coming as it did after three years of scarcity, black-markets and ill-conceived controls, it is hardly surprising that the sudden burst of activity in the summer of 1948 should have been hailed as a miracle demonstrating the efficiency of a market economy if it is allowed a rational framework within which to work." (p. 73)

Note: The report quoted was published in 1953. Had it appeared 7 years later, it could have added that West Germany under policies of free enterprise continued to prosper. The rate of economic growth exceeded that of any other nation by a wide margin.

In 1950, when a government dedicated to free enterprise was functioning in West Germany, American aid was reduced to half that of the preceding year, in 1951 to one-third, and in 1952 was decreased to a token amount. In contrast with more than $3,000,000,000 spent trying to make West Germany function in a straitjacket of price controls and rationing, less than one-third that amount was given to the West German Republic in the succeeding 3 years. And in contrast with aid given to the avowedly Socialist Labor Government in England and totaling more than the war damage there, West Germany's total amount was less than one-tenth of its wartime damage.

These considerations invite questions like those at the end of the report on Great Britain. The pattern of events again raises the question whether too many United States officials in policymaking positions were dedicated Socialists with little understanding of or loyalty to the economic foundation of their own Republic.

France

From 1944 to 1958 under the Fourth Republic, 26 successive governments attempted to cope with what can be described as planned perpetual chaos. Early in the 14-year period, the Socialists nationalized the principal banks and insurance companies, railroads, airlines, merchant shipping, coal mines, utilities, much of the munitions industry, and the larger automobile manufacturers. Creeping inflation had become a way

of life in France prior to World War II, and it was resumed in the postwar years.

But the kaleidoscopic sequence of events in France followed a discernible pattern. Here was socialism in action, usually abetted by the strong Communist minority (at times more than a fourth of the voters) who realized full well that socialism is the "half-way house" to communism. Short of an outright Communist dictatorship of the proletariat, Karl Marx himself hardly could have hoped for a more determined effort to apply his theories.

Compared with the ruin in Germany, the war damage in France was small; nor was there any question of feeding several million refugees or alleviating other hardships beyond the capacity of the French Government to solve. Nevertheless, we provided aid on a large scale and continued it long after aid to Britain and West Germany was drastically curtailed.

Specifically, aid to France in the 8 years from 1948 to 1955, inclusive, totaled nearly $4,000,000,000 and in 1955 was still $402,000,000 in a single year. This total was all in the form of nonmilitary grants; thus it was in addition to the approximately equal sum for military aid, military installations, etc. Including the military aid, grants and credits to France approximated $1,000,000,000 per year.

Finally the turmoil and chaos within France became unbearable. After a series of crises bordering on civil war, the people and their representatives accepted De Gaulle virtually as a dictator. For years, all during the planned chaos while creeping inflation and socialism were draining the economic lifeblood of France, De Gaulle was waiting for the call to serve his nation. Almost certainly, if American aid to the Socialist Government of France had been curtailed earlier, the failure of socialism would have hastened the return of De Gaulle to power.

Why did policymakers in the State Department of the United States persist in prolonging the life of the Socialist Fourth Republic at a four-times greater cost to the United States than the cost of helping the free-enterprise government of the West German Republic? Were the American officials such dedicated Socialists themselves that they were incapable of learning from the obvious lesson provided by West Germany?

Underdeveloped Nations

Now the United States is urged to provide more aid to the underdeveloped countries of the world. India provides a representative as well as a major example.

So little developed, from the modern industrial viewpoint, is India that the situation is almost unimaginable to most people of Western

civilization. Fewer than one in five of the population can read or write; three-quarters of the Indian people live on small farms, where, after paying the landlord his major share of their meager crops, they barely subsist from one harvest to the next.

Lacking incentive for accumulation of even as little capital as would purchase a hoe (increased crop yields would simply raise the rent), the Indian peasant applies primitive methods and obtains the lowest crop yields known in the world. This is not because of the niggardliness of nature. Vast areas are wonderfully fertile, and the climate permits more than one crop per year in much of India; but primitive methods produce crops only one-fifth to one-tenth of those available by better methods.

Starvation of thousands in India is commonplace, even in good years; and when insects or drought damage crops in large areas, millions have starved to death in a single season. Warmhearted people the world over are horrified by these facts of life and death in India and leap to the unwarranted conclusion that the population is excessive in relation to the potential food supply. By the present-day Malthusians, India is regarded as a classical example of overpopulation; but India is not overpopulated in relation to the potential, nor even to the presently available, food supply. About 155,000,000 head of cattle (almost half a cow to every Indian) are sacred to Hindus and not available for food yet are supported on land that could produce some food for the people. India is poverty-stricken and underdeveloped, not because it is overpopulated in relation to the potential or even the available food supply, but because social conditions that the Indians themselves could control discourage accumulation of capital, inhibit the use of available food, and foster ignorance, superstition, and continued degradation of major segments of the populace.

The government of India is in the hands of the Congress Party headed by Mr. Nehru. This political party is determined to make socialism the economic system of India. The Imperial Bank of India, the commercial airlines, the life insurance business, and others have been nationalized. The government is engaged in a series of 5-year plans following Russia's example and plans to control much of heavy industry, the utilities, railroads, etc. Nehru repeatedly has emphasized his belief in socialism and on January 18, 1958, asserted, "There is no return from the goal of socialism in India."

The example of Russia and China also is being followed in agriculture. A Congress Party resolution on January 9, 1959, proposed the gradual transformation of India's 612,000 villages into farm cooperatives, with appropriate "inducements" for any peasants reluctant to join.

What has been the United States response to these developments?

Simply to pour out funds on an increasing scale in a fruitless effort to counterbalance the economic follies of the Indian Government and thus to support socialism at whatever cost to the American people.

The record is obscured by the various means used to give American dollars and goods to India. Direct aid in the form of grants (gifts) ostensibly has been only $310,000,000, but this does not include $1,300,000,000 worth of agricultural commodities, $950,000,000 loaned and to be loaned by 1961 from the International Bank for Reconstruction and Development, $120,000,000 from the Development Loan Fund, $20,000,000 from the Asia Development Fund, $225,000,000 from the Export-Import Bank and Development Fund, and a $400,000,000 loan over a 4-year period proposed by the World Bank in 1957. Thus the United States already has contributed, directly or indirectly, a substantial part of $3,325,000,000 and is committed in one way or another for much of the remainder.

Eighty years ago, Florence Nightingale indicted the empire-builders of England in her book, *The People of India.* She asserted, "The saddest sight to be seen in the East — nay, probably in the world — is the peasant of our Eastern Empire." The peasants of India are a long-suffering lot; they are used to poverty and privation. But is that any excuse for what the United States is doing? Can we do no better for the people of India than substitute a Socialist straitjacket for the oppression of the absentee landlords and empire-builders of an earlier day? Are all our foreign-aid policymakers doctrinaire Socialists who either have forgotten or never have understood what an approach to economic freedom accomplished in our own country? Are they incapable of learning from the "miracle" of West Germany's recovery and current economic growth?

India has long had its intellectual followers of Jefferson and the American ideal. Their writings reveal an understanding of the economic principles expressed and implied in our own Constitution and an eagerness to apply in India the principles that have fostered rapid economic development wherever they have been applied.

In the light of the facts as reported, in the knowledge of our own experience and that of West Germany, is not the United States of America betraying the best interests of the Indian people when it supports socialism for India?

Noteworthy in passing is that $1,041,000,000 of foreign aid has been given to nations in Central and South America, including Cuba, Bolivia with its Communist-dominated government, and Panama. In addition, the Communist satellite nations under Russia's domination have been given more than $2,000,000,000.

As for the defense aspects of foreign aid, a report prepared by

the Legislative Reference Service of the Library of Congress asserts, "It seems clear from the foregoing summary of military aid operations and strategy in the non-European areas that the United States is not training and equipping these forces to play an important local role in an all-out nuclear war between the superpowers. The security of the non-NATO countries in such a war would appear to depend even more than that of the NATO powers upon the ability of the United States to survive a nuclear attack and strike back effectively at the Soviet Union."

Conclusions on Foreign Aid

As economists we desire to emphasize relative priorities for use of the Nation's resources. In recent years, much concern has been expressed about the inadequacy of our public schools and the need for a great increase in the capacity of colleges and universities. Foreign aid since World War II has been six times the value of all the buildings and endowment funds of all colleges and universities in the United States; it has been three and one-half times all the expenditures for new schools in the United States since World War II.

We suspect that some policymakers concerned with foreign aid are dedicated Socialists. We suspect that a predilection for Government operation and control is an "occupational disease" of members of the great bureaucracy administering foreign aid. Indeed, how could the situation be otherwise? Anyone who believes that economic development can best be planned and administered from the top, in spite of the historical record and in disregard of advice from leading anthropologists, must be ignorant of our Nation's economic development since the days of the starving Plymouth colony, ignorant of our Government's failures in attempting to foster economic development among its wards, the American Indians, and ignorant of the West German economic "miracle." Only the abysmally ignorant could be so arrogantly confident of their power to direct economic development by Socialist means.

For what they may be worth, we offer our answers to the questions raised at the beginning of this chapter. The general tendency of American foreign aid has been to foster socialism. The economic results have not been those desired by the American people. Some of the administrators probably are dedicated Socialists, and many others are ignorant of the economic results from such programs. Our friends may survive American aid; but if they do, it will be because they somehow escape from the Socialist straitjackets into which we are trying to force them.

What is the answer? Discontinue most foreign aid, set matters right in our own country as an example to the rest of the world, and encourage those to learn who wish to do so.

VIII.

CAN OUR REPUBLIC SURVIVE?

Many thoughtful citizens, concerned for the future of their children and grandchildren, are asking, Can our Republic survive? Such citizens have learned that inflation is the great destroyer of organized societies; and they know from the lessons of history, including events during their own lifetimes, that republics have been especially vulnerable to the destructive influences of inflation.

For instruction one need not rely on obscure accounts of that classic example, the decline of Rome. There are many more recent examples. France now is struggling to maintain the Fifth Republic, the fifth since our own was begun; Germany has its second republic since World War I; since the liberation of Central and South American countries from Spanish rule in the 19th century there has been a succession of republics and dictatorships, a record that emphasizes the vulnerability of some republican forms of government.

Rare exceptions have occurred. Switzerland has preserved representative government for nearly 500 years, except for temporary interludes. The Republic of Iceland, or at least a representative form of government there, has existed since the tenth century. However, there is little hope that the United States will follow the example of these two exceptions to the general rule. Already the divergence of political-economic developments in the United States from those in Switzerland is so great as to justify present fears for the future of the United States.

The lessons of history teach that at least two conditions are needed for survival of a republic. The first is social and economic progress in a civilization; not even one republic has outlived the decline and fall of any of the several civilizations that are known to have arisen and subsequently declined. The second condition is wise choice among divergent policies when that choice is crucial to survival.

Requirements for a Progressing Civilization[1]

Many of the traits, actions, and emotions of man are exhibited by the lower animals; but man, no matter how low in the human scale,

[1]This portion of the discussion is extracted and in part paraphrased from Henry George, *Progress and Poverty,* Book X, "The Law of Human Progress." Although written more than 80 years ago, this section of the world-famous book on economics is so up-to-date that most of it might have been written recently with the aid of modern anthropological studies of man in society. A modern edition of this American classic is available from the Robert Schalkenbach Foundation, 50 East 69th Street, New York, price $1.50.

has one characteristic of which no animal shows the slightest trace, a clearly recognizable power of improvement, which makes him the progressive animal. Man, wherever we know him, exhibits this power of supplementing what nature has provided by the increasing fruits of successful inquiry.

The varying degrees in which this faculty is used cannot be ascribed to differences in original capacity; the most highly improved peoples of the present day were savages within historic times, and we meet with wide differences between peoples of the same stock. Nor can they be wholly ascribed to differences in physical environment; the cradles of learning and the arts are now in many cases occupied by barbarians, and within a few decades great cities have risen on the hunting grounds of wild tribes. All these differences are evidently connected with social development. Beyond the veriest rudiments, man improves only as he lives with his fellows. Men improve as they become civilized, or as they learn to cooperate in society.

A view now widely held is that the struggle of existence, in proportion as it becomes intense, impels men to new efforts and inventions; that this improvement and capacity for improvement is transmitted by heredity, and extended by the tendency of the best adapted individuals and the best adapted or most improved tribe, nation, or race to survive in the struggle between social aggregates.

But this theory of progress, which seems so natural to us amid an advancing civilization, is disproved by an enormous fact, the fixed or petrified civilizations. The difference between the savage and the civilized man may be explained on the theory that the former is as yet so imperfectly developed that his progress is hardly apparent; but how, on the theory that human progress is the result of general and continuous causes, shall we account for the civilizations that progressed so far and then stopped? It cannot be said of the Hindu and the Chinese, as it may be said of the savage, that our superiority is the result of a longer education; that we are, as it were, the grown men of nature, while they are the children. The Hindus and the Chinese were civilized when our ancestors were savages, but while we have progressed from this savage state to twentieth-century civilization, they have stood still. If progress be the result of fixed laws, inevitable and eternal, which impel men forward, how shall we account for this?

In truth, nothing could be further from explaining the facts of history than the theory that civilization is the result of natural selection operating to improve and elevate the powers of man. That civilization has risen at different times in different places and has progressed at different rates is not inconsistent with this theory, for that might result from the unequal balancing of impelling and resisting forces. But that

progress has commenced everywhere (for even among the lowest tribes it is held that there has been some progress) and has nowhere been continuous but everywhere, in all preceding civilizations, has stopped or retrogressed, is inconsistent. For if progress operated to fix an improvement in man's nature and thus to produce further progess, though there might be occasional interruption, yet the general rule would be that progress would be continuous, that advance would lead to advance and civilization develop into higher civilization.

Not merely the general rule, but the universal rule, has been the reverse of this. The earth is the tomb of dead empires, no less than of dead men. Instead of progress fitting men for greater progress, every civilization that was in its own time as vigorous and advancing as ours is now, has of itself come to a stop. Over and over again, art has declined, learning sunk, power waned, population become sparse, until the people who had built great temples and mighty cities remained but as mere barbarians, who had lost even the memory of their ancestors' greatness.

This universal fact, as soon as it is recognized, disposes of the theory that progress is by hereditary transmission. Throughout history the line of greatest advance does not coincide for any length of time with any line of heredity.

Influence of Social Custom

Whether the mind of any newborn infant is to be English or German, American or Chinese, the mind of a civilized man or the mind of a savage, depends on the social environment in which it is placed. Take a number of infants born of highly civilized parents and transport them to an uninhabited country. Suppose them in some miraculous way to be sustained until they come of age to take care of themselves, and what would you have? More helpless savages than any we know of. They would have fire to discover; the rudest tools and weapons to invent; language to construct.

And reversely, suppose a number of savage infants could, unknown to the mothers (for this would be necessary to make the experiment a fair one), be substituted for as many children of civilization, can we suppose that growing up they would show any difference? Surely, no one who has mixed much with different peoples or classes will think so.

The assumption of great physical improvement in the race within any time of which we have knowledge is utterly without warrant. We know from classic statues, from the burdens carried and the marches made by ancient soldiers, from the records of runners and the feats of gymnasts, that neither in proportion nor strength has the race improved within two thousand years. But the assumption of mental improvement, which is even more confidently and generally made, is

still more preposterous. As poets, artists, architects, philosophers, rhetoricians, statesmen, or soldiers, can modern civilization show individuals of greater mental power than can the ancient? There is no use in recalling names; every schoolboy knows them.

In short, the explanation of the differences that distinguish communities appears to be this: That each society, small or great, necessarily weaves for itself a web of knowledge, beliefs, customs, language, tastes, institutions, and laws. Into this web, woven by each society, or rather into these webs, for each community above the simplest is made up of minor societies, which overlap and interlace each other, the individual is received at birth and continues until his death. This is the way in which customs, and religions, and prejudices, and tastes, and languages, grow up and are perpetuated. This is the way that skill is transmitted and knowledge is stored up, and the discoveries of one time are made the common stock and steppingstone of the next. Though it is this web that often offers obstacles to progress (as in India today), it is what makes progress possible. It enables any schoolboy in our time to learn in a few hours more of the universe than Ptolemy knew; it places the most humdrum scientist far above the level reached by the giant mind of Aristotle. It is to the race what memory is to the individual. Human progress goes on as the advances of one generation are secured as the common property of the next, and made the starting point for new advances.

Essential Conditions

When men live separately, the whole powers of a man are required to maintain existence; mental power is set free for higher uses only by the association of men in communities, which permits the division of labor and all the economies that come with the cooperation of increased numbers. And as the wasteful expenditure of mental power in conflict becomes greater or less as an equality of rights is ignored or is recognized, equality of opportunity (or justice) is the second essential of progress. Thus association in equality of rights is the essential condition of progress. Association frees mental powers for expenditure in improvement; and equality, or justice, or freedom (for the terms here signify the same thing) prevents the dissipation of this power in fruitless struggles.

Civilization is cooperation. Union and liberty are its sponsors. The great extension of association, including the growth of larger and denser communities, the increase of commerce with the manifold exchanges that knit a community together and link it with other though widely separated communities, the growth of international and municipal law, the advance in security of property and person, in short the

recognition of equal rights to life, liberty, and the pursuit of happiness, these make our modern civilization so much greater, so much higher, than any that has gone before.

Just as social adjustments promote justice, just as they acknowledge the equality of right between man and man, just as they ensure to each the perfect liberty that is bounded only by the equal liberty of every other, must civilization advance. Just as they fail in this, must advancing civilization come to a halt and recede.

Many American citizens seem to have forgotten or perhaps never have realized what kind of society the Constitution of the United States provided for under the conditions then existing. To describe this society, the American ideal and plan, as stated and implied in the Constitution, we refer again to the national objectives that we listed on pages 10 and 11.

And for those unfamiliar with the Nation's history or who have difficulty in learning a lesson that extends over a century and a half, we repeat that the economic "miracle" of West Germany's postwar recovery and economic growth provides a lesson more readily grasped. Abandonment of Marxian Socialist policies and adoption of relatively free competition were followed, in the short span of a few years, by economic growth startling in its magnitude to all who were ignorant of or had lost faith in the principles of free enterprise and voluntary cooperation outlined above.

Choosing Among Policies Crucial for Survival

Many people seem to assume that a republic (or a "democracy" as republics are too generally misnamed) functions somewhat as follows:

a. That the two principal political parties, although each includes many "ward heelers" and similar politicians of low grade, are dominated by two groups of leading statesmen who usually advocate their two different views on controversial questions crucial to survival.

b. That the citizens, especially in those republics where general public education is the rule, wisely elect their representatives, after ascertaining what the candidates' views are, and thus, in effect, make known the citizens' decisions on major questions.

c. That the elected statesmen then proceed by appropriate legislation to steer the ship of state on the course indicated by their previously announced policies.

However, anyone who chooses to look carefully at what actually occurs will find little resemblance to the a-b-c description given above.

Although the following discussion requires the use of various phrases such as "politicians," "spoils of office," etc., we neither condemn nor approve by using such emotionally loaded words. Moreover, we

are not trying to arouse the emotions of readers. Neither as cynics nor as Pollyannas but as scientists of the social scene, we are endeavoring to report on the facts of political-economic relationships. Our indebtedness to Arthur F. Bentley will be apparent to readers specializing in this field.[2]

We should describe the actual functioning of a republic somewhat as follows:

1. The basic fact, regardless of the appearance as reflected in numerous "splinter" political parties, is that there are two powerful groups of professional politicians in a republic, the "ins" and the "outs." (Hereafter in the discussion we shall use the names Ins and Outs for the two groups.) The Ins are those who currently enjoy the lion's share of perquisites, power and pay; and the Outs are those who have to "make do" with what is left.

2. The basic and continuous struggle, the permanent major political issue, in a republic is between the Outs who "want in" and the Ins who are determined to retain the spoils of office. This is the issue, the only basic issue of permanent and great concern to the professional politicians of both major parties.

3. An occasional prominent man in either party may be a statesman. ("Statesman" is our name for an individual so well-informed as to have useful views on questions crucial to the republic's survival, so courageous that he will follow the dictates of his understanding, and so careless of reelection that he will vote as he thinks best for the republic.) Although there is a widespread popular notion that all important politicians should be statesmen, the lessons of history indicate that, if the survival of republics had been dependent on the existence of major parties composed largely of statesmen, there would be no republic surviving today. In short, statesmen neither are numerous nor are they assured of political longevity; they are "rare birds" (no pun intended) who only occasionaly can make the weight of their opinions felt.

4. As for the citizens of a republic, evidently most citizens vote according to inherited or early-acquired prejudices. Relatively few citizens will trouble to inform themselves on public questions: in fact, most lack the basic education as well as the will to inform themselves adequately on vital public issues in this age so complicated by rapid scientific advance. If the survival of a republic depended on adequately educating a *majority* of the citizens, no republic could long survive.

5. How then can a republic survive? It can survive when a relatively well-informed minority of the public holds the balance of elective power between the Ins and the Outs and uses that balance of

[2]Arthur F. Bentley, *The Process of Government*, The Principia Press, Bloomington, Indiana, 1955.

power judiciously. Politicians survive in office not by great erudition or firm convictions as to what is best for the republic, but by winning elections; and elections are won by getting a few more of the independent votes than those given to the opposition. Hence the assiduous attention paid by all politicians to minority groups: to the farmers benefiting from price supports who number fewer than 1 in 60 of the voting population, to the foreign-background minorities each of which is seemingly insignificant in voting power, and to numerous other groups that may weigh in the balance of power. The politician naturally thinks first and foremost of winning the election; he is well aware that a defeated politician has little influence; he puts what he considers first things first and strives by all not obviously dishonorable means to get elected.

At first thought, some readers who accept this description of events may doubt that a republic can survive. We believe, however, that a quite different conclusion is justified. Precisely because the professional politicians function as they do, there is reason to hope that an informed and independent minority can ensure our Republic's survival.

Today in the United States the relatively well-informed and independent voters (independent in voting even if registered as Ins or Outs) constitute a powerful minority able to wield the balance of power in most Congressional election districts.[8] Given enough unbiased and scientific information on questions crucial to the Nation's survival, this strong minority can safeguard the Republic.

To this end, no new leaders are needed. Seeking supermen statesmen whose erudition, courage, and self-sacrifice might save the Republic would be a waste of time. Not enough such men, if they could be found, could possibly be elected to Congress; in many districts where political "bosses" rule, such men could not even be nominated; their high characters would be an insuperable disqualification. But even the most powerful city "boss" is vulnerable in one respect: his nominee must be elected and reelected if the "boss" is to retain his power and perquisites.

That politicians want above all else to know the desires of the informed and independent minority is clear. Before campaigns, "trial balloons" in the form of various news releases keep appearing from Washington. In the spring of 1960 Nixon, for example, was considering policies that would appeal to the "liberal" middle-of-the-road Republicans and Democrats; or Nixon was being urged by Goldwater and others to pay more heed to the conservative Republicans; Nixon was working on a farm

[8]The most one-sided presidential election of the present century was that of 1936 when Roosevelt obtained 523 electoral votes. Nevertheless, the shift of only 1,119,500 votes in 17 States would have resulted in the election of Landon. The States concerned were those where the results were closest and represented 52.3 percent of the population.

program; Nixon was concerned about the medical plan for the aged, etc., etc. Obviously those "trial balloons" were intended to reveal the direction and strength of the political winds.

We do not imply that Mr. Nixon or any other popular politician lacks deep-seated convictions; he apparently is like the more able politicians of the opposite party. They as well as he know that convictions too firmly expressed on controversial issues are a luxury that professional politicians cannot afford. Until the desires of the balance-of-power independent minority are revealed, how can any political leader know in what direction he must lead?

No new political organization is needed. Individual citizens and small neighborhood groups who make their desires known by letter or other communication will find eager listeners among their politician friends and representatives. Above all else, a professional politician wants to know the answer to this question: In what direction should I lead in order to obtain your vote. In effect he is saying, "Remember, I have no irreversible personal convictions, at least none that will interfere with my doing your bidding; please tell me what you want so that I may keep my job." Also important for the independent minority to remember is that this is the professional politician's viewpoint not only in early November of even-numbered years but 365 days of every year.

The only question is whether the informed and independent minority will take the trouble individually and personally to make known their views. In that connection they might well reflect on the resolution and devotion of those who persevered in the trying times of the American Revolution to make possible the founding of our Republic. They too were a minority at first. Today's informed and independent minority should realize that failure to function as an independent balance-of-power not only would betray their children and grandchildren but also would betray the one best hope of all mankind. If and when our Republic declines and falls, that will mark the end of Western civilization.

IX.

ECONOMIC ASPECTS OF A SURVIVAL PROGRAM

In a popular book a professor has described his view of the American scene from his ivory tower.[1] He sees what he calls an "affluent" society consisting in large part of families so rich in money and poor in judgment that they demand their automobiles be tail-finned monsters in order to keep one step ahead of the Joneses in their ostentatious spending. Concluding that the average family cannot be expected to spend its income wisely, this professor proposes that taxes be increased further in order that wiser heads in the Government service may buy for the public what the professor and others like him think the public should have.

Now that the compact cars are proving to be so much more popular than the tail-finned monsters, one can understand more readily what has happened in recent years. The many billions of inflationary purchasing media created during World War II by the monetization of Government debt and more recently by the monetization of rapidly increasing private debt made possible an increasing demand for automobiles at rising prices. As automobile manufacturers discovered in the seller's markets after the war that they could sell more and more cars, the styling and design personnel not unnaturally assumed that their efforts accounted for the increased sales. Thus styling modifications were carried to weird extremes, abetted to some extent by the preferences of some beneficiaries of inflation who had more money to spend than ever before.

After a few years, the average citizen was confronted with a difficult choice when he needed a new car. Either he could take a tail-finned monster or he could buy a foreign car, with room too restricted for most American families, and run the risk of not having needed parts readily available. That millions of citizens were dissatisfied with the finned monstrosities soon became evident, when American Motors first succeeded with its Rambler; and the public's preference became undeniable as compact cars attracted an increasing percentage of new-car buyers.

Our conclusion is that most of the American public never did demand the tail-finned monsters and that those uneconomical and, to many,

[1]John Kenneth Galbraith, *The Affluent Society,* Houghton Mifflin Company, Boston, 1958.

ungraceful automobiles were one of the indirect effects of a great inflation. Moreover, we believe that professors in ivory towers who jump to conclusions without inquiring more thoroughly into the reasons for what they observe also are unwitting victims of a great inflation. In a sense, they are the intellectual tail fins of modern society.

Coming Down to Earth

Even a casual walk through the less prepossessing residential areas of great cities (South Boston, for example, or Harlem or numerous other areas north, south, east, and west) should enable any keen observer to realize that by far the most of United States citizens are not "affluent." If such practical coming down to earth from their ivory towers is too mundane for the professors who think they could spend the public's money to better advantage, they might at least peruse the Federal reports of income-tax returns. The table on page 81 shows what they would find.

We urge readers to study carefully the table of family incomes after Federal income taxes. The number of families shown in the first column corresponds to the income brackets for which the Government reports gross incomes, taxes, etc. in detail. We used data for 1957 because that is the latest year of general prosperity for which data are available.

Several significant features merit emphasis:

1. The top one-sixth of America's 40,000,000 families, measured by income left after Federal income taxes, had an average monthly income of $857 ($198 per week).

2. Five-sixths of all families, more than 33,000,000, had incomes ranging from $612 per month ($141 per week) for the most prosperous 5 percent down to $100 per month ($23 per week) for the least prosperous 3.8 percent of all families.

3. More than half of 40,000,000 families had less than $400 per month ($92 per week).

4. About one-fourth, 24.7 percent or nearly 10,000,000 families, had less than $260 per month ($60 per week).

5. Nearly one-seventh of American families had less than $200 per month. For families in this group that included 2 adults and 3 children, the income per capita averaged only $36.60 per month ($8.45 per week).

Such are the facts. Readers can judge for themselves how "affluent" America's 40,000,000 families are. Knowing your own expenditures, you can readily judge the circumstances of at least those immediately above and below your own group in the table. We believe that the following conclusions are justified by the facts shown:

FAMILY INCOMES AFTER FEDERAL INCOME TAXES

(For 40,000,000 American Families in 1957)

Number of Families	*Av. Monthly Income After Taxes*	*Per Capita Income (4 in family)*	*Per Capita Income (5 in family)*	*Percentage of Total Families*	*Cumulative Percentage*
1,510,000	$100	$ 25.00	$ 20.00	3.8%	3.8%
1,660,000	143	35.75	28.60	4.2	8.0
2,010,000	183	45.75	36.60	5.0	13.0
2,200,000	216	54.00	43.20	5.6	18.6
2,440,000	256	64.00	51.20	6.1	24.7
2,680,000	298	74.50	59.60	6.7	31.4
2,980,000	330	82.50	66.00	7.4	38.8
2,970,000	355	88.75	71.00	7.4	46.2
5,590,000	417	104.25	83.40	14.0	60.2
4,310,000	483	120.75	96.60	10.8	71.0
3,020,000	550	137.50	110.00	7.5	78.6
1,990,000	612	153.00	122.40	5.0	83.6
6,400,000	857	214.25	171.40	16.0	100.0

Notes: 1. State and local income taxes totaled $1,767,000,000 and reduced further, in many States, the spendable income of families.

2. Totals are affected to a negligible extent by rounding the figures.

3. Social Security taxes reduce the average monthly income after taxes by another 3 percent in most instances.

a. More than half of all the families in the United States do not have enough income left after taxes to save for their children's higher educations without sacrificing some features of decent living.

b. This half of America's families have no margin facilitating saving for emergencies such as serious illness.

c. At most, only 20 percent of America's families can hope to accumulate savings on a scale sufficient to cover both higher education for their children and family emergencies. Only a small portion of this fortunate 20 percent can be called "affluent" in that they have a comfortable margin of income over all foreseeable needs.

Highest Economic Priorities

In view of the actual situation, we believe that an increase in the present annual $600 exemption of income before taxes to at least $900 should have first priority. A family of 5 then could receive as much as $375 per month before being subject to Federal income taxes (although subject to Social Security taxes and in many instances to State income taxes).

The loss in taxes to the U. S. Treasury would approximate $8,000,000,000 annually. However, that sum left in the hands of American families would enable them in their own localities so solve the Nation's school problem at the grammar and high schools levels (without the waste necessarily involved in having the Federal Government collect the funds and give part of them back to local school districts), would enable them to save more for the higher education of their children, and would enable far more of these families to accumulate funds for emergencies. (The required curtailment of Federal spending is discussed subsequently in this chapter.)

Second in priority we place means for alleviating the situation of American colleges and universities. These institutions of higher learning should be paying better salaries in order to attract and keep the most desirable personnel, and they must have more funds for other operating expenses if they are to provide the increased facilities needed for the Nation's youth. In our judgment, the most urgent first step is to facilitate increases in tuition fees without adding to the burden on families whose children are in college and on young men and women who are earning their way in college. We recommend making all payments of tuition to accredited colleges and universities deductible from income before taxes. Thus all colleges that deemed such a step necessary could increase tuition fees about 20 percent without increasing the actual cost to those paying the bill.

Many people apparently do not realize that we tax young people who are earning their way in college about 10 percent of their earnings.

In view of the urgent need for maximum education of our youth, this situation is a disgrace to the Nation. The combined effects of increasing the personal exemption to $900 and allowing all tuition payments as deductions from income before taxes would eliminate the taxation of virtually all young people who are earning their way through college.

The cost to the U. S. Treasury of making college tuition fees deductible from income before taxes would approximate $250,000,000. Although this sum is small as Federal receipts and expenditures go, we believe that it has a far higher economic priority from the viewpoint of most citizens than do many present Federal expenditures.

Stimulating Economic Growth

One of the most important problems that the Nation confronts is stimulation of economic growth. Because such growth is not characteristic of all businesses at all times, the Nation as a whole enjoys the benefit of economic growth only when the expansion of growing businesses more than counterbalances the relative contraction of businesses that, for any of several reasons, may be unable to grow rapidly, may be stabilized, or even may be dying. Above all, each of the small businesses having great growth potential should be permitted to grow at the greatest possible rate, and the soundest way to accomplish this result is to let them use their profits for growth instead of for the Federal bureaucracy.

We recommend that the corporation tax on small businesses be eliminated, that there be no corporation tax on any business until profits exceed $100,000 in any one year, and that the maximum corporation tax be reduced to less than 50 percent as soon as possible. By eliminating taxes on corporations having incomes less than $100,000, the Treasury would lose only about 9 percent of the present corporation income tax. In the hands of the nearly 530,000 corporations concerned, this sum (about $1,900,000,000) could be far more effective in stimulating the Nation's economic growth than any other single influence we can imagine. Not to be overlooked is the great saving in clerical work that should result by reducing the number of corporation tax returns to only 6 percent of the present number.

At present many individuals of outstanding ability in organization and management of business enterprises are taxed so heavily as to destroy the incentive for full use of their abilities. We refer not to the relatively few very highly paid executives in the business world whose salaries run into the hundreds of thousands of dollars. Apparently the abilities of those individuals are used to the maximum extent. We refer rather to the far more numerous businessmen whose earnings

are much less, probably in the $20,000 and upward range, and who either retire early or simply decline to seek better opportunities to use their abilities because the odds are so heavily weighted against them by present tax laws. Why should any man who is comfortably situated on annual earnings of, for example, $40,000 (perhaps $25,000 net after taxes) exert himself to obtain more when Uncle Sam will take nearly two-thirds of the additional earnings or even more?

The U. S. Treasury recently has estimated that if the highest income-tax bracket were 50 percent the revenue loss would be only $780,000,000. We recommend that on earned incomes the maximum rate be 50 percent, and that early consideration be given to further reduction of the maximum tax on earned incomes. We estimate that the cost to the Treasury of this change would not exceed $400,000,000 annually. The actual cost to the Treasury certainly would be less to the extent that individuals who are not now producing at full capacity increased their earnings and the earnings of the businesses with which they are or become associated. In fact, we should not be surprised if a net gain rather than a loss in taxes resulted from this change.

Savings in Expenditures

Even if it be assumed that no offsetting gains to the Treasury would occur, the losses of tax revenue indicated above would total no more than $10,550,000,000. We shall now show how much greater savings in Government expenditures can be effected.

Certainly among the lowest priority expenditures of the Federal Government are the subsidies to special interests, especially those that do not remedy but actually aggravate the problems they purport to solve. Outstanding in this classification are the various agricultural subsidies and "benefits."

The Federal budget for the fiscal year 1961 estimates agricultural expenditures at $5,623,000,000, more than double the expenditures only 7 years earlier. Nearly $4,000,000,000 is scheduled for farm price supports and related programs. We recommend an immediate reduction of appropriations for agricultural purposes to $623,000,000. All of the price support programs should be eliminated, as outlined in Chapter VI; and other expenditures should be drastically reduced to the levels of a few years ago. Estimated savings: $5,000,000,000.

The natural resources section of the national budget contemplates increasing expenditures in 1961 for land and water resources to $1,440,000,000 compared with $803,000,000 in 1956. Surely no harm would result from postponing more development of irrigated lands until a need for additional farming areas rather than a surplus is foreseeable.

Immediate reduction to the 1956 level is recommended, and further curtailment may be advisable. If the income possibilities from the use of Government forest and recreation areas were better exploited, appropriations could readily be reduced to the 1955 level. Estimated savings in these categories: $700,000,000.

Expenditures under the labor and welfare classification have increased more than $2,000,000,000 since 1954. By reducing them to the 1958 level, we believe that nothing having a higher economic priority than the tax reductions we have proposed would be sacrificed. Estimated savings: $1,200,000,000.

In the general classification, veterans' services and benefits, one subdivision of expenses (not including veterans' disability compensation but including pensions and allowances) has increased from $751,000,000 in 1954 to $1,774,000,000 proposed for 1961. An immediate reduction to a roughly 50-percent increase for the period, say to the 1959 level, is recommended. Estimated savings: $700,000,000.

Under the general Government classification, the cost of property and record managment has skyrocketed from $155,000,000 in 1954 to the $432,000,000 proposed for 1961. Judicious elimination of unnecessary records and sales of property not needed should make possible substantial savings. Other savings in this general category are possible. Estimated savings: $250,000,000.

The foreign aid portion of the budget is divided among several major categories. We believe that a more judicious use of military assistance permitting prosperous European nations to pay for their own defense and eliminating military aid to some South American, Caribbean, and other nations under military dictatorships would save $1,500,000,000. Curtailment of the general foreign aid program in order to avoid putting friends in Socialist straitjackets would save $2,000,000,000. Estimated savings: $3,500,000,000.

In the general category of commerce and housing, the 1961 budget is more than 3 times that of 1954 and is nearly double that of 1957. We recommend reduction to the 1956 level and transfer of space exploration expenditures to the national security classification. Exclusive of the latter change, which would provide no savings, the estimated savings would be $750,000,000.

That at least 6 or 7 percent of the proposed expenditures for national security could be saved seems probable. For a few years such savings could be effected by the sale of obsolete or no longer needed materials that have been stockpiled since World War II in a program noteworthy for stupidity and inefficiency. Reorganization of the Defense Department to provide a technical staff responsible directly to the Secretary of Defense and depending on him for future

promotion probably would result in great savings, because duplication of effort in the three competing services could be decreased. Estimated savings: $2,700,000,000.

In only two years, the interest on the public debt has increased nearly $2,000,000,000. Return to the gold standard, thereby assuring the future buying power of money invested in Government bonds, and consistent planned retirement of the debt at an average rate of at least $5,000,000,000 annually soon would lower the interest rate on the debt. Within a year or two, the amount indicated could be saved, and further savings would accrue thereafter. The Nation's experience when the gold standard was resumed after the Civil War was relatively even more favorable and demonstrates the results to be expected. Estimated savings: $2,000,000,000.

The potential savings described above total $16,800,000,000. However, the tax reductions we have recommended total $10,550,000,000. Therefore, as soon as the indicated reductions in expenditures could be effected, $6,250,000,000 would be available annually for reducing the Federal debt. This provides a substantial margin over the $5,000,000,000 annual debt reduction that we estimate would be sufficient to reestablish the credit of the United States on a firm foundation with resulting lower interest costs. Even more important, such debt reduction would facilitate refinancing the debt in order to distribute maturities over the decades ahead and remove the threat of insolvency under adverse developments, a threat implicit in the huge total of short-term debt.

Obviously, adoption of these recommendations would not solve all the economic problems of the United States, but it would greatly increase the probability that at some distant future time most American families might correctly be described as "affluent." In the meantime, and of far greater importance, the actions that we have recommended are, we believe, first-priority steps in a survival program. They would help our Nation to gain time in which to develop the further policies, economic and political, domestic and foreign, that will be essential to survival of the United States and of Western civilization.

X.

COPING WITH THE AMERICAN CRISIS OF THE 1960's

The problems analyzed in this book are economic problems inasmuch as questions concerning the most effective use of the Nation's resources, human and other, are involved. That the crisis problems also have political aspects is apparent, but we expect that sound economic solutions will be adopted when understanding of such solutions is sufficiently widespread among the independent minority of voters who hold the balance of power in national elections. We can imagine no other practicable means by which a republic can hope to choose wisely among the alternative courses of action crucial to survival.

The economic problems concerned not only have political aspects, but also have what may be called human interest aspects. The poverty, hunger, and disease prevalent in India arouse in every man of good will a desire to improve the lot of the Indian peasant. The plight of those American farmers who are not sharing in the general prosperity inclines their sympathetic fellow citizens to undertake what is intended to be helpful action. The depressing conditions found in the slums of great cities arouse in many Americans both indignation and a determination to remedy such situations.

That the strong emotions thus aroused can serve a useful purpose is undeniable. The world would indeed be a poor place for habitation if there were not many Good Samaritans among us.

Nevertheless, the history of humankind proves that strong emotions of sympathy and a desire to do good are not enough. Too often the emotional urge to action stimulates a hasty and unwise choice of means for solving problems of men with the result that a problem is aggravated rather than solved. Such hasty and ill-advised choices of means usually are satisfying at first to those eager to do good, because they feel that something is being done, but too often are disastrous in the long run for the victims of uninformed good intentions.

What then is needed in order to choose effective means of solving the problems of men in society? The first requisite is adequate analysis of each problem situation. A sufficient answer should be sought to the question, How does it happen that this problem exists? Until that ques-

tion can be satisfactorily answered, action intended to remedy the situation probably will do more harm than good, judging by the extensive experience of mankind.

Modern Methods of Inquiry

Long ago men learned to seek answers to such questions in order to solve their problems pertaining to inanimate things. The revolution in methods of inquiry represented in the work of such men as Galileo more than 300 years ago marked the beginning of man's effective search for useful solutions. The results of that procedure have been the great technological advances that continue on an increasingly effective scale today.

In solving the physiological problems of men the new methods also proved applicable. Doctors eventually stopped bleeding patients and refused to act until they had found better answers to the question, How have these symptoms of illness come to exist? This revolution in the practice of medicine no doubt was at times distressing to relatives who pleaded for drastic action to save their loved ones, but many more patients survived.

The accumulating evidence clearly indicates that a similar application of intelligent analysis to the behavioral problems of men can provide useful solutions instead of disastrous consequences. But the first order of business for all who would alleviate the social ills of mankind, if their efforts are to be effective in the long run, must be to find satisfactory answers to the question, How does it happen that these problems exist?

By way of illustration and in order to present a useful analysis of a major problem of our times, we turn to the problem of inflation. A principal symptom of inflation, perhaps the consequence most widely observed, is the general rise in prices that has reduced the buying power of the dollar to less than half that before World War II. However, the name "inflation," when used with technical accuracy as it so rarely is, refers to excessive expansion of the purchasing media used to buy things in the channels of trade.

The purchasing media used in the United States are of two principal types: (1) the currency (paper money and metal coins) carried in one's pockets and passed from hand to hand when purchases are made; and (2) the checks drawn on accounts with the commercial banks by individuals and businesses by means of which such checking accounts (or demand deposits) are transferred from one holder to another. That is, the purchasing media in use include both currency and checking accounts.

Sources of Purchasing Media

Following the procedures of scientific inquiry, we ask these questions: How do purchasing media come into existence in the first place, and how does it happen that an excess of purchasing media over the usual amount required has been brought into use during recent decades? For answers to these questions, we turn to the chart on pages 90-91 that shows the sources of all purchasing media in use. For many readers the captions on the chart will be self-explanatory, but for other readers the following more detailed explanation will be helpful.

The first source of purchasing media is the natural substance (modified by human processing effort) that is chosen as the basic or standard purchasing medium. In the present industrial civilization, the money commodity is gold. In the chart the total U. S. gold stock is shown in two parts: the amount that is in excess of net foreign demand claims, and the amount subject to such claims. The qualities of this commodity that make it a desirable basic purchasing medium have been recognized for thousands of years.

In spite of the so-called departure from the gold standard, gold is still the money commodity of modern civilization. There is no need here to trace its history, nor to forecast its remote future. For our purpose at this time we need only point out that existing gold held as reserves of the various banking systems actually is being used as purchasing media, although it may circulate in an altogether different form than the gold coins or gold certificates that formerly were available.

Gold, whether produced in the United States or imported, ordinarily is sold to the Treasury. The seller receives a check drawn on the Treasury's account; and (except when a gold sterilization policy was in effect for several months after December 1936) the Treasury counterbalances these drafts against its checking account by depositing certificates representing the gold with the Federal Reserve banks. The effect is the same as though the Treasury first had deposited a certificate representing the gold in the Federal Reserve bank, and had then drawn a check against that bank in the amount of the value of the new gold.

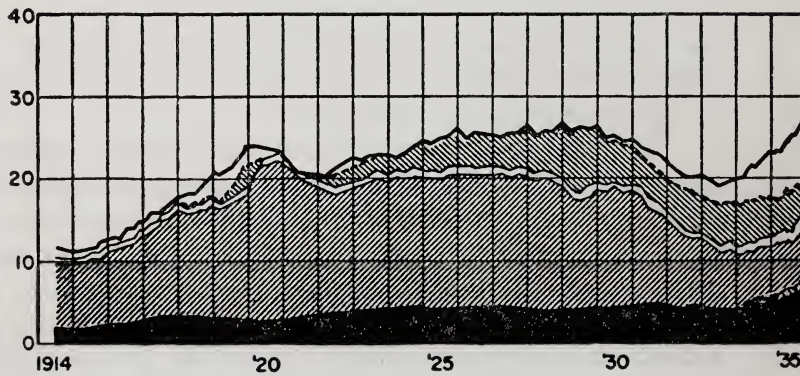
When the seller of the gold deposits the Treasury check for credit to his own account in his local bank, his checking account (demand deposit) is thereby increased. The local bank in turn deposits the Treasury check in the nearest Federal Reserve bank, and thereby increases its reserve account. By this means purchasing media equivalent in value to the gold sold to the Treasury are made available to the seller; and, when he uses the funds to buy something desired, the purchasing media pass

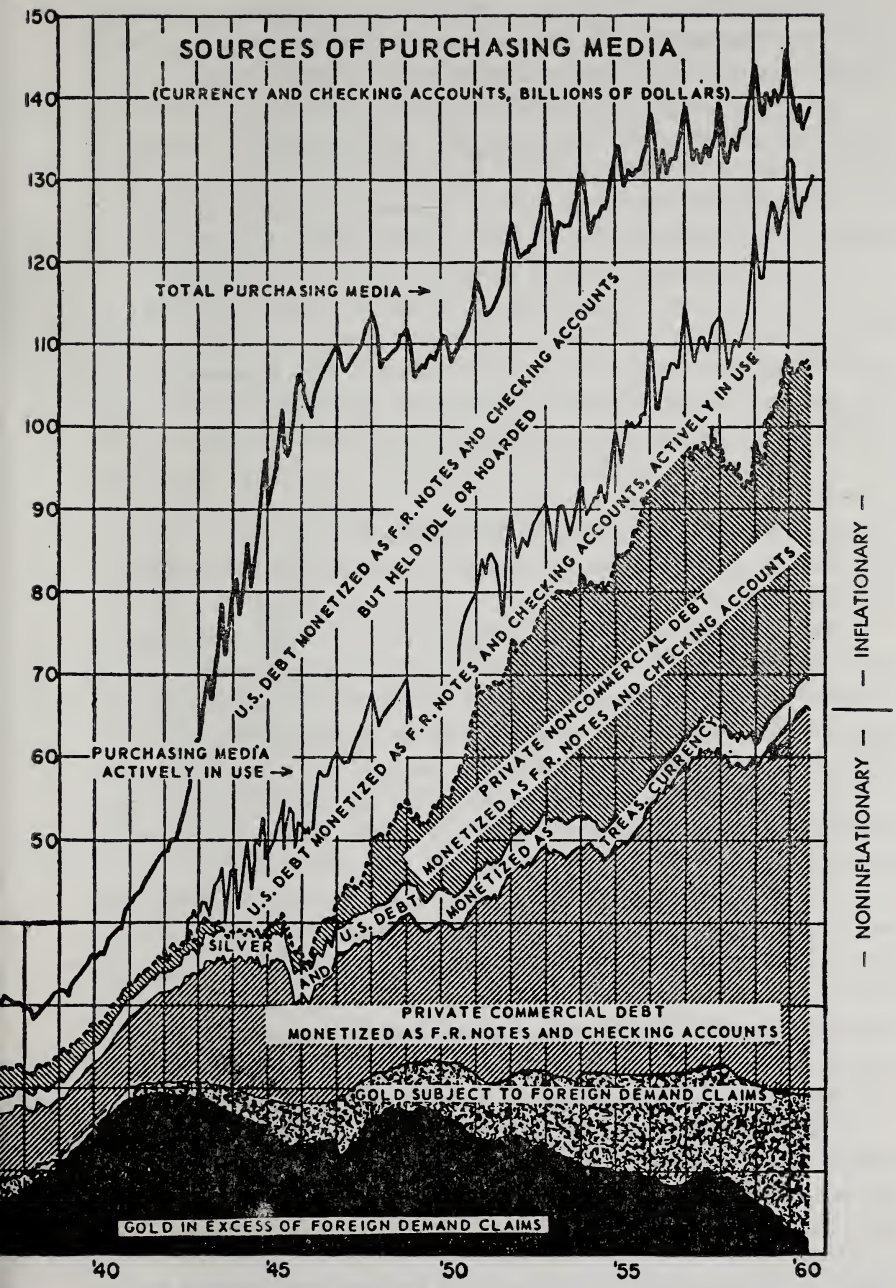
(*Continued on page 92*)

SOURCES
OF
PURCHASING MEDIA

This chart shows the Nation's money-credit record since 1914. Clearly evident are the World War I and World War II monetizations of Federal debt with the resulting creation of excess or inflationary purchasing media. Also apparent are the private credit inflations that followed each World War. Not only was the monetization of Federal debt proportionately greater during World War II than it was during World War I, but also the private credit inflation in subsequent years has been greater in the more recent period.

Note the loss of gold since 1950 and the rapidly shrinking total of gold left after allowing for foreign demand claims against U. S. gold.




SOURCES OF PURCHASING MEDIA
(CURRENCY AND CHECKING ACCOUNTS, BILLIONS OF DOLLARS)
150
140
130
120
110
100
90
80
70
60
50
TOTAL PURCHASING MEDIA →
U.S. DEBT MONETIZED AS F.R. NOTES AND CHECKING ACCOUNTS BUT HELD IDLE OR HOARDED
PRIVATE NONCOMMERCIAL DEBT MONETIZED AS F.R. NOTES AND CHECKING ACCOUNTS, ACTIVELY IN USE
PURCHASING MEDIA ACTIVELY IN USE →
U.S. DEBT MONETIZED AS F.R. NOTES AND CHECKING ACCOUNTS
SILVER AND U.S. DEBT MONETIZED AS TREAS. CURRENCY
PRIVATE COMMERCIAL DEBT MONETIZED AS F.R. NOTES AND CHECKING ACCOUNTS
GOLD SUBJECT TO FOREIGN DEMAND CLAIMS
GOLD IN EXCESS OF FOREIGN DEMAND CLAIMS
'40
'45
'50
'55
'60
— INFLATIONARY —
— NONINFLATIONARY —

on to someone else and thus remain in circulation. (If the reserves of the member bank involved are increased by the new credit to its deposit at the Federal Reserve bank, the member bank is tempted to expand its loans or investments in order to use the excess reserves profitably, thereby increasing still further the purchasing media in circulation.)

A second source of purchasing media is private commercial debt monetized as Federal Reserve notes and checking accounts through the lending function of the commercial banking system. The borrower whose note is discounted receives a credit to his checking account that is not deducted from someone ele's account. He therefore has at his disposal new purchasing media over and above that previously existing.

The third source of purchasing media is the currency issued by the Treasury in the form of silver certificates, United States notes, standard silver dollars, subsidiary silver coin, and minor coin. Because this kind of currency is created by the direct action of the Treasury and does not reflect either an increase of gold or of other products coming to market, the Treasury currency is regarded as inflationary purchasing media. However, in an amount equal to any gold kept idle in the general fund and not used to issue gold certificates, Treasury currency is regarded as non-inflationary, because it in effect represents gold not otherwise represented in the channels of trade.

The fourth source of purchasing media is private noncommercial debt monetized as Federal Reserve notes and checking accounts by the banking system. This results in the creation of new purchasing media based on things that have tangible value or represent tangible values, often much greater than the purchasing media created, but that are not offered on the market during the period of the loan. These are what we have described elsewhere as investment-type assets of the banking system.[1]

The fifth source of purchasing media is the commercial banking system's investment in Federal Government obligations to the extent that such investments exceed the capital and savings accounts of commercial banks that are available for that purpose. We refer to this source as "monetized public debt," because the commercial banks create new purchasing media by increasing the Treasury's checking accounts in exchange for these Federal debt obligations.

Turning now to the chart on pages 90-91, the reader will find that the five sources of purchasing media are differentiated by contrasting shading in order to facilitate understanding. The data shown are for bank call dates during each year prior to June 1933 and monthly thereafter.

---

[1]See E. C. Harwood, *Cause and Control of the Business Cycle,* American Institute for Economic Research (Eighth edition, 1961).

The purchasing media derived from and representing gold in the channels of trade as well as that derived by monetizing commercial debt are *not* in excess of the usual business needs, i.e. are noninflationary. In general, commercial borrowing in the form of short-term automatically self-liquidating loans results in the creation of purchasing media (largely checking accounts) that represent things produced and en route to markets. The new purchasing media thus created facilitate the distribution of such things and are retired from circulation when the things are sold and loans are repaid. Of course, the borrowing and repayments by the millions of businesses in the United States overlap with the result that at all times substantial amounts of such purchasing media are in use.

Purchasing media derived from the other three sources shown are inflationary, that is, are in excess of that needed for the usual business transactions at the usual prices. When some or all of such excess purchasing media are used to buy things in the Nation's markets, the inevitable result is rising prices, because demand exceeds supply at the former price level.

The Situation Since 1940

Since 1940 the amount of inflationary purchasing media created and available for use obviously has increased greatly. By the end of World War II the total approximated $65,000,000,000 compared with noninflationary purchasing media totaling less than $40,000,000,000. If all of the inflationary purchasing media had been actively used by the recipients, the wartime rise in prices would have been far greater in spite of any price controls. (Never in the history of the world have attempts to control prices succeeded when inflationary purchasing media were in circulation, although quality deterioration and other subtle changes sometimes have inclined the unobservant to think that price controls have succeeded for a time.)

As it happened, much of the inflationary purchasing media created and made available for use during World War II was hoarded or held inactive rather than used. Many things such as new automobiles, new homes, and new plant and equipment for most businesses simply were not being manufactured and thus were not available at any price. Consequently, many individuals and businesses chose to accumulate funds for postwar use. In addition widespread fears of a postwar depression induced many businessmen to accumulate idle demand deposits for later use. The artificially low interest rates forced by the Government and the Federal Reserve Board both facilitated inflation and discouraged the more active use by investment of idle currency and checking accounts.

In the years that followed the end of World War II, monetized non-

commercial (mortgage and installment)debt replaced some of the monetized U. S. debt as a source of inflationary purchasing media, and increasing amounts of purchasing media formerly hoarded or held inactive were actively used. By late 1959 the amount of inflationary purchasing media approximated $80,000,000,000 of which nearly $70,000,000,000 was actively in use. The almost continuous increase in the inflationary purchasing media used, from about $10,000,000,000 at the end of World War II to nearly $70,000,000,000 at the end of 1959, accounts for the great rise in prices; it tended to cut short the business recessions of the 1950's (at the cost of increasing the underlying maladjustments); it encouraged the great rise in wages where union labor had monopoly advantages; and it helped to create the distortions now so apparent within our economy and in our trading relations with the rest of the world.

The latter aspect of the situation is reflected on the chart in the increasing amount of the Nation's gold reserve that has become subject to foreign demand claims. So extensive and so prolonged has been the money-credit mismanagement of recent years that the United States has lost its position of great financial strength attained early in World War II and now is confronted with the threat of a "run" on the dollar and inability to meet the legitimate demands of its short-term creditors in the rest of the world.

Of course, there have been many other consequences attributable at least in part to the great inflation of the Nation's purchasing media in the past two decades. The delusions of economic grandeur that have encouraged financial support of Socialist governments abroad are a case in point. Another is the misdirection of economic effort within the United States to the production of tail fins and other products inspired by industrial designers who became overconfident about the part they had played in creating the sellers' markets of the postwar years. Another consequence is the willingness of politicians to inflict on taxpayers the costs of the farm program and other squandering for special interests as well as the apparent willingness of taxpayers to support such programs. Still another is the encouragement of businessmen who have acquiesced in the demands of labor monopolists in the belief that higher prices could be established at will. And by no means the least but perhaps the most damaging of the consequences has been the miseducation of superficial thinkers and glib writers, the intellectual tail fins of modern society, who gaze out from their ivory towers and find in the inflation "numbers game" evidence of great and widespread private affluence, so great that they prescribe for the Nation's "welfare" still more taxes and still more Government spending.

The foregoing explains in large part how the crisis of the 1960's happens to exist. The purpose of this explanation is not to imply that correction of money-credit mismanagement is the only action required

to solve current problems, although that is part of the action required.[2] Rather have we intended to illustrate by example how the search for solutions should proceed.

The Challenge Today

In the 1960 political campaign, one of the major political parties proposed in its platform that the problems of the 1960's be solved by more of the same money-credit mismanagement that set the stage for the Great Depression of the 1930's, the same mismanagement that already had repeated on a larger scale the economic policy errors of World War I and the 1920's. This party's panacea was more spending and artificially induced lower interest rates, which would foster still more inflation.

The other major party seemed similarly unaware of the principal economic policy changes required if great and irreparable damage to the United States was to be avoided. It is true that this party's platform evidenced greater fiscal responsibility, at least it paid lip service to some sound economic principles; but it proposed to aid the farmers more effectively (presumably on a larger scale) as well as to expand other Government spending; and it also provided little evidence that the professional politicians of this party either understood or were prepared to cope with the American Crisis of the 1960's.

Thus we return to what seems to us the only hope for survival of the Republic. If enough of the balance-of-power independent minority take the trouble to inform themselves and make their views known to their representatives in Government, our Nation may regain the main road toward its original goals and ensure its survival.

---

[2]The Nation's experiment with an irredeemable dollar has continued more than a quarter of a century. The pledge of the United States to "pay to the bearer on demand" the number of dollars specified on all currency of $10 or higher denomination has been disregarded for domestic holders of currency during that period. (A dollar is defined by law as one thirty-fifth of an ounce of gold in an alloy nine-tenths fine or pure.)

In effect, the proponents of inflation argue that this pledge should be permanently disregarded. They deny that it is the basic promise underlying as a foundation most of the other innumerable contracts that characterize modern industrial society.

Wholly aside from the moral aspects of the question, on which we do not presume to offer scientific conclusions, we are convinced from the lessons of history that keeping such a promise to "pay to the bearer on demand" is an essential aspect of a sound and useful money-credit system. The nations of the world have experimented extensively with "managed" money, and many nations are so experimenting today. Not yet has such an experiment succeeded in sustaining sound economic growth. Moreover, in instances where some of the most striking failures have occurred, subsequent adoption of a sound currency, directly or indirectly convertible to gold on demand, apparently has contributed to business recoveries and economic growth such as that of West Germany in recent years.

All the weight of evidence suggests that a sound currency redeemable in gold on demand is essential to the optimum functioning of a modern industrial economy. Never has the gold standard failed to serve its purpose except when a nation's money-credit system has been misused by prolonged inflation.

To that end we propose to continue in the years ahead as in the past three decades to publish the results of sound scientific inquiry. The chart showing sources of purchasing media, for example, is one of the fruits of research that has continued since its origination in 1926 by a present member of our staff. The Government never has thus reported to citizens its part in the money-credit mismanagement of recent decades, nor as yet has this information been provided by any other source. Obviously, such information is of vital importance to those who will determine the Nation's economic policies in the years ahead.

In closing our discussion of the American Crisis of the 1960's, an explanation of the Institute's role is appropriate. Many readers have urged that the Institute or members of its staff should participate in national political leadership in order that sound economic policies may be applied. However, we believe that, aside from the legal restrictions on a tax-exempt educational and scientific organization, the roles of scientist adviser and political leader are incompatible. Sound scientific work requires both freedom from bias and willingness to revise theory in the light of new evidence. The political leader not only is subject to the bias induced by seeking personal position and power but also is prone to become the prisoner of past policies.

We repeat that the citizens who are an independent and informed minority hold the balance of political power. On their shoulders, because of the way a republic functions, rests the political responsibility for the future of our Nation and of Western civilization.

Twentieth century commons sens main
330.973A5125tw C.3
3 1262 03293 1007
330.973
A5125tw
C. 3

PUBL TITUTE FOR
ECONOMIC

Booklets

What Will Deflation or More Inflation Mean to You? by the Research, Investment, and Insurance Sections of the Institute under the direction of E. C. Harwood. Price $1.00.

Life Insurance and Annuities From the Buyer's Point of View by William J. Matteson. Price $1.00.

What Will Social Security Mean to You? by William J. Matteson. Price $1.00.

How To Invest Wisely by C. Russell Doane and E. C. Harwood. Price $1.00.

Investment Trusts and Funds From the Investor's Point of View by C. Russell Doane and Edward J. Hills. Price $1.00.

How To Avoid Financial Tangles by Kenneth C. Masteller. Price $1.00.

How To Make Your Budget Balance by Helen Fowle and Margaret Blodgett. Price $1.00.

The Rubber Budget Account Book. Price 25 cents.

Economic Tides and Trends, Their Effects on Your Lifetime Plans by the Editorial Staff. Price $1.00.

Current Economic Trends by the Editorial Staff. Price $1.00.

Cause and Control of the Business Cycle by E. C. Harwood. Price $2.00.

Useful Economics by E. C. Harwood. Price $1.00.

Reconstruction of Economics by E. C. Harwood. Price $1.00.

Twentieth Century Common Sense and the American Crisis of the 1960's by the Editorial Staff under the direction of E. C. Harwood. Price $1.00, 3 copies for $2.00, 10 copies for $5.00.

The First Quarter Century and Plans for the Future, a report on the Institute's past activities and future plans, will be sent free on request.

Periodical Reports

Research Reports. Weekly analyses of economic developments, emphasizing their probable future significance. $6.50 per quarter, $25 per year.

Investment Bulletin. Issued twice monthly at $10 per year and includes:
Investment Plan for those dependent on income from investments,
Speculative-Investment Plan for those who can assume the "businessman's risk,"
Speculative Plan for those who can assume speculative risks.

Economic News. Published nine times a year. Nontechnical articles on current economic problems. $1 per year, $2 for three years, $3 for five years.

Annual Sustaining Membership

An Annual Sustaining Member receives all publications currently available including the annual revisions of books. $9 per quarter, $35 per year.